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Politics this week

Mar 21st 2002
From The Economist print edition

Truce, anyone?

AP

America's vice-president, Dick Cheney, wound up a tour of the **Middle East**, leaving an envoy, Anthony Zinni, behind in Israel to coax Israel and the Palestinians into a truce before next week's Arab summit meeting in Beirut. Israel withdrew from some Palestinian areas, but suicide bombers struck lethally in northern Israel and Jerusalem. President George Bush said he was "frustrated" with the continuing violence and urged the Palestinian leader, Yasser Arafat, to curb it.

See article: America and the Arabs

Following Robert Mugabe's rigged re-election as president, **Zimbabwe** was suspended from the Commonwealth. Nigeria and South Africa backed the decision, which marks the first time these influential African states have condemned Mr Mugabe unambiguously. Mr Mugabe promised to carry on seizing white-owned farms regardless. His cheated rival, Morgan Tsvangirai, was charged with treason.

See article: Africans tire of Robert Mugabe

Summit for everyone

Meeting in Barcelona, the **EU's leaders** promised (again) to make their markets virtuous, but not just yet. Laggard France was ready to free its energy market only for non-domestic customers, from 2004. But the EU's controversial Galileo global satellite-positioning system got the go-ahead, as did, from 2004, a play for unified air traffic control.

See article: The EU's so-so summit on liberalisation

Serbia and Montenegro agreed to stay together in a looser federation that would no longer be called **Yugoslavia**. But Montenegro would be entitled to hold a referendum on independence, if its government wished, in three years' time.

See article: In a tricky new deal, Yugoslavia may cease to exist

Germany's ruling Social Democrats, whose chancellor is seeking re-election this autumn, were embarrassed by a scandal over a waste-disposal contract in the North Rhine-Westphalian city of Cologne.

France's would-be president, Lionel Jospin, promised *euro*18 billion ($16 billion) of tax cuts over the five-year term; higher capital gains tax; lower taxes on housing; more public housing; and 900,000 fewer unemployed. He also called for "genuine European economic government" within the euro area to counterbalance the European Central Bank.

A top economic adviser to **Italy's** government, Marco Biagi, was murdered in Bologna. Italy's prime minister, Silvio Berlusconi, urged trade unions to call off a planned general strike and to discuss the controversial labour-market reforms that Mr Biagi had recommended.

See article: Political murder in Italy

A ship towed into a Sicilian port disgorged some 1,000 would-be **immigrants**,

mostly Kurds. Italian authorities said more ships were on the way. Umberto Bossi, leader of the populist Northern League, which is part of the government coalition, caused a stir by saying that the ship should have been turned away.

Reuters

Rejecting their Socialist government, **Portugal's** voters gave the centre-right Social Democrats a margin of just over 2% of the votes but no overall majority of seats in parliament. Likely outcome: a coalition including the right-wing populist People's Party.

See article: Portugal's probable weak new government

At least three-quarters of **Gibraltar's** population of 32,000 demonstrated against a plan still being negotiated by the British and Spanish governments that is likely to suggest shared sovereignty over the Rock, along with financial sweeteners from the EU worth *euro*60m ($53m) for new infrastructure and development.

Sending reinforcments

Britain agreed to a request by the United States to send 1,700 commandos to **Afghanistan** to help root out Taliban and al-Qaeda fighters. The Americans were reported to have found the rebels more numerous, tougher and better armed than was first thought.

Reuters

See article: Rebuilding Afghanistan

Five people, among them the wife and daughter of an American diplomat, were killed in a terrorist attack on a church in the **Pakistani** capital, Islamabad.

See article: Pakistan's Christians

Sri Lanka's ruling party won a resounding endorsement for its efforts to bring an end to the war with the Tamil Tigers. It swept all but five of 222 village and city councils in elections billed as a referendum on the peace plans.

Christine Tsung, the first woman to head **Taiwan's** economics ministry, resigned after opposition and government legislators complained that she lacked the ability to guide the economy as it tries to recover from recession.

In the latest of a series of protests in **China's** “rust belt”, in the industrial north-east, several thousand workers laid off by state firms in Liaoyang and Daqing took to the streets complaining of unpaid salaries and welfare benefits.

Swift departure

Jane Swift, the embattled governor of **Massachusetts**, decided not to seek re-election, clearing the way for Mitt Romney, the organiser of the Salt Lake Olympics, to get the Republican nomination in the traditionally Democratic state.

Congress finally passed a **campaign-finance bill** which clamps down on “soft” money given to parties, as opposed to individual politicians. George Bush says he will sign it.

America moved towards introducing **military tribunals** for al-Qaeda suspects. The proceedings will be similar to court martials, with laxer rules of evidence than civilian courts.

The Bush administration moved towards merging the **Customs Service** with the **Immigration and Naturalisation Service**, which includes the Border Patrol. The move, which requires congressional approval, is supposed to beef up homeland security.

See article: Reforming the Immigration and Naturalisation Service

The administration decided not to “certify” that **North Korea** is complying with a 1994 agreement to freeze its nuclear programme. However a waiver should allow $95m-worth of oil to go to North Korea this year in an effort to encourage co-operation with international inspectors.

Terror in Peru

A powerful car bomb exploded near the United States' embassy in Lima, **Peru's** capital, killing at least eight people and injuring up to 40. The blast occurred three days before George Bush was due to visit Lima, as part of a Latin American tour.

See article: Peru's shaky democracy

In **Colombia**, gunmen killed the archbishop of Cali, the country's third city, as he was leaving a church. He had criticised guerrilla kidnappings, but also politicians financed by drug traffickers.

See article: The massacre of Colombia's trade unionists

Officials of the IMF continued to insist that **Argentina** must carry out further reforms, including amending laws on bankruptcy and “economic subversion”, before the Fund would restore its loan programme to the country.

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Business this week

Mar 21st 2002
From The Economist print edition

The shredding of Andersen

The future of **Andersen** in America looked bleak after it was charged with obstructing justice by shredding documents related to Enron's audit. Andersen's units outside America continued intensive merger discussions with KPMG, another “big five” accountant. However, PricewaterhouseCoopers struck a deal with Andersen's partners in Hong Kong and China.

See article: More post-Enron trouble for Andersen

As counting began in the vote on a merger between **Hewlett-Packard** and **Compaq Computer**, HP's boss, Carly Fiorina, claimed a narrow victory for the $20 billion bid. Walter Hewlett, leader of the anti-merger faction, was less certain: he said the vote was “too close to call”.

See article: The HP-Compaq merger

EMI, the world's third-largest music group, announced plans to slash its workforce by 1,800—18% of the total—and said it was dropping underperforming rockers. It is unlikely to be as generous to departing staff as it was to Mariah Carey, a Canadian warbler recently paid $28m to terminate a contract barely a year old.

Philipp Holzmann, one of Germany's biggest construction companies, was on the brink of bankruptcy after protracted negotiations with creditors finally broke down. The company got *euro*2.2 billion ($2.3 billion) two years ago in a bail-out organised by Gerhard Schröder, Germany's chancellor, but looks to have run out of luck this time.

See article: Europe's fear of bankruptcies

Slimming down

France Telecom announced a *euro*8.3 billion ($7.4 billion) loss for 2001, the second-largest ever by a French company. France Telecom has written off *euro*10.2 billion of acquisitions made during the bubble years.

Deutsche Telekom shocked investors by cutting its dividend and announcing that its debt mountain would remain stubbornly high. Debt-reduction plans are set back by a year because of Deutsche Telekom's failure to sell its cable-TV business and a reluctance to float its mobile division while the market continues to languish.

Bulge-bracket investment banks suffered some slimming down. **Goldman Sachs** saw profits fall by 32% in the latest quarter compared with a year ago to $524m. Big mergers and acquisitions and flotations are scarce. Rival **Lehman Brothers** made a profit of $298m, down 23% in the same period.

Japan's **Mitsubishi Electric** and **Hitachi** announced a merger of most of their chip operations to become the world's third-largest chip-maker. Two more loss-making Japanese chip makers, **Toshiba** and **Fujitsu**, also said that they were discussing a chip-making alliance.

Meanwhile, another attempt to reduce overcapacity in the industry plodded on. America's **Micron Technology** and South Korea's debt-laden **Hynix** were said to be inching closer to a deal to create the world's biggest maker of memory chips.

Travel talk

EADS, Airbus's parent company, said that profits would be down this year and refused to forecast orders for 2003 because of doubts following the shock to the world's airlines caused by September 11th. It also announced profits last year of *euro*1.4 billion ($1.3 billion), compared with a loss of *euro*909m the year before. However, the results were bolstered by a full consolidation of Airbus into the company's accounts.

Ryanair won a court case in Germany allowing it to advertise as flights to Frankfurt those landing at Frankfurt-Hahn, an airport some 100km from the city. Lufthansa, which brought the case against its no-frills rival, had previously secured the right to append Frankfurt to Hahn airport's title when it used the place for cargo flights; passengers are now upgraded to equal treatment.

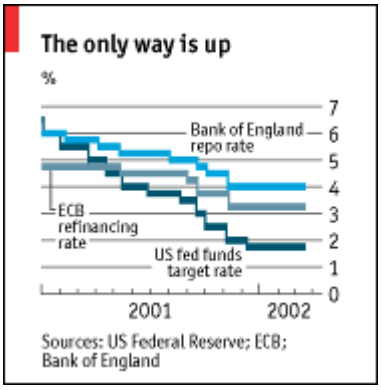
Another American incursion into South Korea was beset by uncertainty. **General Motors'** $400m take-over of Daewoo Motor seemed under threat after differences emerged over contingent liabilities and opposition from Daewoo's hardline unions.

The Wallenberg family quietly slipped behind the wheel at **Scania**, a Swedish firm that makes top-of-the-range lorries. Upping its voting stake to 19.5% allows the Wallenbergs to side with either Volvo or Volkswagen, both big shareholders, to create a majority that could vet any prospective purchaser.

Rates of change

It looked as if the cycle of **interest-rate cuts** around the world has come to an end. America's Federal Reserve shifted its stance to judge the threat of inflation as the same as the risk of the economy weakening, hinting that interest rates would rise as the economic recovery gathers pace. Sweden and New Zealand set the tone and raised rates.

See article: Is the economy going too fast again?



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The war against terrorism

America and the Arabs

Mar 21st 2002
From The Economist print edition

Why not democracy?

HE MAY have heard something different in private. But in public the various Arab allies Dick Cheney called on during his tour of the Arab world this past fortnight had a unanimous message for the vice-president. Whether or not they accept that Saddam Hussein is part of an “axis of evil”, they do not favour and will not support a renewed American attempt to remove him by force. At their summit in Beirut next week, Arab leaders will say so again, urging America to work on Palestine instead. This circling of the Arab caravan may not save Iraq's dictator; America is in no mood right now to let other countries veto actions it deems vital. All the same, Mr Cheney's dusty reception suggests that America needs to think again about how to work with the Arabs.

Friends can have honest differences. Many of America's European allies have expressed similar qualms about picking a new fight with Saddam. And being nearer to Iraq gives countries such as Saudi Arabia, Egypt and Jordan more to fear if things go wrong. But among Arabs another factor is also at play. Though not as brutal as former Soviet clients such as Iraq and Syria, the Arab regimes America is friendliest with are not democracies themselves. Worse, all are perceived on the fabled Arab “street” as owing their survival to the economic or military support of the United States. If an American attack on Iraq were to provoke a flood of popular outrage, they risk being washed away. This turns them into timid and fragile allies at the very moment the United States most needs them to be bold and durable ones.

A wild surmise

If the Americans were to think afresh about how to work with the Arabs, they could do worse than to ask themselves a radical question. Why should America not start to make the case for Arab democracy? Plainly, the United States cannot afford to push this idea too fast. This is a region of wounded sensibilities, whose people will not take kindly to westerners imposing their own way of running things. Such a change could easily be counter-productive for the West. In Saudi Arabia, the democratic alternative to the conservative Islamism practised by the House of Saud might turn out to be a reactionary Islamism of the sort championed by Osama bin Laden.

For just this sort of reason, western policy towards the Arabs has long been governed by realpolitik. Like the British before them, the Americans have preferred stability to uncertain experiments with democracy. Doesn't stability have to be paramount in a region that contains so much of the world's oil? And who is to say that democracy suits Arabs anyway? They appear to have rubbed along happily without it for long enough. So, at any rate, say the realists. But, like a lot of conventional wisdom, it may not be so very realistic at all.

The Iranian revolution of 1979 pointed to the danger of depending on military bases and the friendship of totalitarian regimes. Propping up such regimes can have the paradoxical result of weakening them by making them seem less legitimate. When they collapse, the former propper-up is not usually much loved by the formerly stamped-upon. Besides, America cannot risk concentrating exclusively on the sort of security that military power buys it. In the longer run, its influence is liable to depend at least as much on what Joseph Nye of Harvard University calls “soft” power: the ability, as he puts it, “to get others to want what you want” (see article).

Piety and pretext

To a greater extent than Americans and Europeans sometimes realise, the West already wields a good deal of this soft power in the Arab world. The average youngster in Cairo or Damascus enjoys fizzy drinks, soap operas and designer labels no less than the average youngster in Paris or New York. But something else that Arabs may want has so far been denied to them: a chance to choose their own leaders by holding proper elections, just as westerners do. The terror of September 11th appeared to expose deep religious and cultural divisions between the Arabs and the West. Might democracy one day become a unifying ideal both can share?

The kings and despots who run the Arab world dismiss this as a dangerous fantasy. That is no surprise: most have much to fear from genuine elections. More surprising is the existence in the West of a whole industry of intellectuals and diplomats dedicated to exposing the preposterousness of the very idea. These experts invoke any number of sophisticated reasons why the Arabs are unsuited to democracy.

Foremost is the argument from religion. Islam in its classical form allows no separation between religion and state; *sharia* law is ordained by God; men who propose framing their own laws (ie, politicians) are therefore apostates. Then comes the argument from history. Many of the Arab states that emerged from the Ottoman empire inherited borders that owed less to a well-shaped sense of nationhood than to the administrative convenience or strategic calculation of the great powers. In such countries, people identify strongly with their tribe or clan, and with a wider Arabhood or Islamic fellowship, but only weakly with the state. Holding such a state together therefore requires a strong and usually repressive power at the centre. Last is the argument from tradition. Political parties and ballot boxes are understood in the West. In the Arabian peninsula, the people and their rulers are still quite comfortable, thank you, with time-honoured methods of quasi-consultation (see our survey of the Gulf states).

These things may complicate the growth of democracy in the Arab world. Yet they are no excuse for failing to try. If Islam is inimical to democracy, somebody should tell the Turks and the Iranians, who in markedly different ways just beyond the Arab East are exercising the muscles of pluralist politics. The argument from history is a fraud: in Asia and Africa, fissiparous states carved from former empires have nonetheless turned themselves into democracies. As for tradition, this may prolong the reigns of the kings and emirs of the rich Gulf Lilliputs. But in bigger countries—and over the past 20 years, the Saudi population has zoomed from 9m to 22m—"tradition" has been fortified by a strong dose of repression.

Those who consider Arab democracy a fantasy should ask how long the existing system can last

Those who consider Arab democracy a fantasy should ask how long the existing system can last. The Arabs have not rubbed along happily without democracy; they have rubbed along unhappily without it. In single-party Syria, the appetite for open politics is keen. In multi-party Egypt, voters are incensed by the fact that opposition parties are tolerated but prevented from winning elections, even for control of a toothless parliament. When offered a real chance to vote, Arabs have accepted with gusto. The obstacle has not been religion or tradition, but—as, calamitously, in Algeria a decade ago—the refusal of those in power to accept the people's verdict. With ballot boxes blocked, no wonder opposition flows towards the mosque, the only institution no Arab regime dares ban.

America cannot change the Arab world at a stroke. It will not risk knocking the legs away from longstanding allies such as Egypt and Saudi Arabia. In wars hot and cold, great powers have collected allies where they can, without too much scruple. But the struggle against the forces unleashed by Mr bin Laden is a most unusual war. Because his aim was to lure the West into an internal quarrel about the future of the Muslim world, it is in large part a struggle about values. The West must not impose its values, but needs to say out loud that its own achievements of religious tolerance and liberal democracy are not just luxuries to be consumed at home. They are universal ideals that can, and should, be welcomed by Arabs too.

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India's Hindus and Muslims

After Ayodhya

Mar 21st 2002
From The Economist print edition

Let the ruling party shun Hindus who have brought religious violence back into politics

Get article background

AP

IN THE end, a degree of sanity prevailed. The militant Hindus who had vowed to breach a police cordon and start the work of building a temple to the god Ram at the disputed site of Ayodhya decided to respect a Supreme Court decision barring them from the area. So charged have Hindu-Muslim relations in India become in recent weeks, as the declared deadline of March 15th neared, that a clash at Ram's supposed birthplace might well have provoked bloodshed on an appalling scale across the nation. It has, unfortunately, happened often enough before.

But the threat has not vanished. The court's decision is only an interim one, and the main Hindu groups have not given up on their quest to build their temple. Extreme religious violence, which seemed in recent years to have faded after the Ayodhya-related explosion of 1992-93, is again a feature of the political landscape. Though faults lie on both sides (it was a Muslim attack on Hindus in a train in Gujarat that started the recent slaughter), the great bulk of victims were, as always, Muslims. Once again, educated Hindus are to be heard inveighing against the “appeasing” of Muslims through such concessions as separate constitutional status for Kashmir or the right to practise Islamic civil law. Once again, the police are being accused of doing little or nothing to help Muslim victims of rampaging Hindu mobs. Once again, India's 130m Muslims feel unequal and unsafe in their own country. Far too many Hindus would refuse to accept that it is “their own country” at all.

The wonder of it, perhaps, is that things are not worse. While the world applauds Pakistan for at last locking up the leaders of its extreme religious groups, in India the zealots still support, sustain and to a degree constitute the government. The BJP, which leads the ruling coalition, was founded as a political front for the Hindu movement. It is simply one, and by no means the dominant, member of what is called the Sangh Pariwar, the “family of organisations”. Other members of the family are much less savoury. There is the VHP, the World Hindu Organisation, which led the movement to build the Ram temple. There is the Bajrang Dal, the brutalist “youth wing” of the VHP. There is substantial evidence that members of the VHP and the Bajrang Dal helped to organise the slaughter of hundreds of Muslims in Gujarat after 58 Hindus were killed on a train as they returned from Ayodhya.

And there is the RSS, a militaristic mass organisation of Hindus whose members drill in khaki at sunrise, and salute the saffron flag. It was a former RSS member, Nathuram Godse, who assassinated Mahatma Gandhi for “betraying” India by permitting the creation of Pakistan. The RSS passed a repugnant resolution only last weekend, declaring that the safety of India's Muslims depended on the goodwill of the majority—rather than, say, the rule of law. Most of the BJP's top people, including its moderate leader and prime minister, Atal Behari Vajpayee, have been members of the RSS. In few other democracies is the ruling party so explicitly associated with such unacceptable partners.

Mr Vajpayee's defenders often claim that he would like nothing better than to ditch the VHP and the Bajrang Dal, and turn the BJP into a modern, secular party. Perhaps: but there is too little evidence of his trying to do it, and even less of his succeeding. Indeed, there are good grounds for worrying that the reverse is true. Faltering in the polls, and having just lost control of Uttar Pradesh, India's largest state, the BJP faces the loss of Gujarat, its last stronghold, in elections next year. Powerful voices within the party insist that the reason for this is that the party has gone soft on its agenda of *Hindutva*—Hinduness. To them, the solution is obvious: shout about issues such as Ayodhya and bait the Muslims whenever possible. The dismal consequences can be seen on the streets.

The BJP rode to power in the early 1990s on a tide of religious bigotry, exploiting the Ayodhya issue for electoral gain. One of its senior figures, L.K. Advani, made the Ram campaign his own, and used to give speeches beneath a flag that showed India as a single saffron block—with pre-Partition boundaries and Pakistan swallowed up inside “India”. Mr Advani is now India's home-affairs minister, and presumptive successor to the ailing Mr Vajpayee. As such, he is responsible for the rule of law in India. After Gujarat, he should be leading a drive to crack down on the people who organised the atrocities. India's standing as a secular democracy may depend on it.

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Airline insurance

Sky-high risks

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A better way to insure airlines against terrorist acts

AP

AFTER the terrorist attacks in America last September, terrorist risk became the pariah of perils. The airline industry was most directly affected by the attacks, and it was the first to find that no one wanted to insure terrorist risk. Insurance companies immediately increased premiums and cut cover for airlines' third-party terror and war liabilities to $50m per airline, per “event”. Under pressure from airlines, the American government and the members of the European Union agreed to become insurers of last resort for airlines' war and terrorist liabilities, for a limited period. These government guarantees are due to expire at the end of the month.

On the runway

The American government has already agreed to extend its guarantee for another 60 days. The EU's transport ministers are meeting next week in Brussels to decide what to do. Insurers and reinsurers are keen for the commercial market to resume the provision of all airline insurance as soon as possible. No wonder: the premiums for such cover have inevitably increased considerably. Besides, there is a broader point: experience with a wide range of risks, from nuclear power stations to housing developments on flood plains, suggests that it is usually a mistake for government to step in and protect private commerce from carrying the full costs of the risks it incurs.

However, in the case of terrorism, and especially of terrorism in the skies, a number of special factors arise. Some are purely practical: a disaster as sudden and unforeseen as the attacks on the World Trade Centre has had devastating effects on the insurance industry. The maximum cover for third-party terrorist risk available in the primary aviation market is now $50m, and that is not nearly enough to cover risks that are perceived to be much higher since September 11th. Even if the market could offer sufficient cover, another catastrophe on such a scale would be more than the market could cope with. Last year's events have pushed insurers and reinsurers to the limit. The total cost of the attacks is now estimated to be $60 billion, more than a quarter of the total capitalisation of the reinsurance industry that carries most of the burden.

In addition, a rare and devastating risk of a political nature is arguably one that it is right for governments to cover, at least in part. In the wake of attacks by Irish terrorists the British government has recognised this point by agreeing to back a mutual fund to cover risks to property from terrorist attack.

In the case of the airlines, the appropriate answer is some form of mutual scheme with government backing. In fact, under the code-name “Equitime”, representatives of airlines, insurers and the American government are setting up an insurance vehicle to be financed by airlines and reinsured by the government. The Association of European Airlines wants a similar scheme: a mutual fund for European airlines financed by a levy on every airline ticket. Governments would guarantee the fund's excess risk, but their role would diminish as the fund grew. Eventually a European fund could even be integrated into a global one. A third plan, proposed by the London Market Insurance Brokers Committee, would establish a global insurance fund for airline terror, to which airports and the firms that lease planes would also contribute.

Setting something up will take time. So, to bridge the gap, governments will have to remain insurer of

last resort for airlines' war and terrorist risk for some time to come.

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Colombia and the United States

Fighting Colombia's guerrillas

Mar 21st 2002
From The Economist print edition

America should offer its weapons, but not its soldiers, to shore up democracy in Colombia

Get article background

AP

IT IS a world away from Afghanistan. But this week American officials were preparing to step up action against three other groups on their list of "international terrorist organisations"—in Colombia. Done the right way, this could help eventually to bring peace and to strengthen democracy in Latin America's third most populous country. But there are many dangers, not least that of conflating Latin American guerrillas, however nasty, with Islamic terrorists.

Originally Marxist, the struggle of Colombia's two guerrilla groups, the FARC and the ELN, has become one of plunder. Financed by kidnapping, extortion and taxes on the drug trade, the FARC, in particular, has grown into a powerful army even as its political support has all but evaporated. Guerrilla violence has called forth its mirror image, in the bloody paramilitary vigilantes of the United Self-Defence Forces of Colombia (AUC), who enjoy the collusion of some army officers.

The Clinton administration gave a dollop of military aid to Colombia, to train a new army brigade and equip it with helicopters. But this aid has been subject to a restriction: it is supposed to be used to fight illegal drugs, not guerrillas. Now, George Bush wants Congress to lift that restriction, and to approve fresh aid, to protect an important oil pipeline and the electricity grid from guerrilla sabotage.

Two things have prompted this proposed widening of American help. One is that Colombia's president, Andres Pastrana, has lost patience after talking to the FARC for three years, during which the guerrillas showed no signs of wanting peace. Last month Mr Pastrana called off the talks, a move that has been met by a wave of guerrilla sabotage attacks. He was prompted in part by polls suggesting that in next May's presidential election war-weary Colombians will choose Alvaro Uribe, who wants tougher military action against the FARC. The second change is that many people in the United States have begun to view Colombia's conflicts through the prism of September 11th. This has revived America's appetite for fighting against insurgencies in foreign countries.

The Americans should be wary of making this link. Unlike al-Qaeda, the FARC poses no direct threat to the security of the United States. And if there is one thing that inflames Latin Americans more than the perceived neglect of their region by their mighty neighbour (see article), it is over-heavy-handed American "intervention". That is why Mr Bush would be wise to rule out sending combat troops to Colombia.

With that proviso, the case for further American (and, for that matter, European) aid to Colombia is a strong one. It stems from the failure of the rich countries' attempts to prohibit cocaine and heroin. Each year, drug consumers unwittingly stuff $500m-800m or so into the pockets of the FARC and the AUC. It is only fair to help Colombia's democracy to defend itself—and right that aid should no longer be restricted to a counter-productive and doomed effort to wipe out drug supplies.

But, if aid is to be directed openly against the guerrillas, it should have a clear purpose, and come with the right message. This is something George Bush could deliver on his trip this weekend to Latin America. The aim of American policy should be to strengthen Colombian democracy and its associated

However much foreigners help, the main effort

has to come from Colombia itself

institutions. Military training, more helicopters and more intelligence are all needed. But so are more and better policemen and prosecutors, to establish the rule of law. Nor is the FARC democracy's only enemy. The AUC kills at least as many civilians (see article), and is more deeply implicated in the drug trade than is the FARC. That makes a first-ever drug-trafficking indictment against three FARC commanders issued by the Justice Department this week look politically contrived. And it means that America should press Colombia much harder to take on the AUC, and to punish army officers found to have helped it.

However much foreigners help, the main effort has to come from Colombia itself. Its people now appear to realise that they can no longer live side-by-side with violence. It is wrecking their economy and their society, as well as taking a terrible toll of lives. It may be an illusion to imagine, as Mr Uribe and some American officials seem to, that the FARC can be eliminated. A more realistic aim is to weaken it so that it is more serious about peace when talks resume, as they will eventually have to. But even that limited aim is a worthy one.

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About sponsorship

Britain's public services

That dangerous stage

Mar 21st 2002
From The Economist print edition

Tony Blair's government is looking wobbly in the area which matters most to voters

Getty Images

FOR Tony Blair, the outside world is a place of moral certainty. There are good guys and bad guys, and what needs to be done is pretty clear. Home, by contrast, is a messy sort of place, where the prime minister's job is not to uphold eternal values but to force through some unpopular changes that may make the country work a bit better. So if, as Britain despatches 1,700 marines to help finish off the bad guys in Afghanistan, Mr Blair cuts a more impressive figure abroad than he does at home, it is not surprising.

Mr Blair's government is at that dangerous stage. The gloss of last year's landslide has worn off; the next election is too far away to foster unity among the Labour Party and its allies; fighting the battles that need to be fought seems like hard work. No wonder Mr Blair is looking so wobbly.

The area where this is most obvious, and where it matters most, is the public services. Mr Blair faces a difficulty here which is partly of his own making. By focusing his last election campaign on the need to improve hospitals, schools, transport and policing, he built up expectations. And he has been admirably frank about how that improvement needs to be achieved. A lazier and more cynical prime minister might have blamed past failure on Tory underfunding, thrown some more money at the relevant ministries and hoped for the best. Mr Blair has said many times that reforms in the way the public services work need to go alongside increases in cash.

The trouble is that public services are, for the most part, people—teachers, doctors, nurses, policemen—so reforming them means changing working practices. People don't much like having new ways of working foisted on them, and their unions (the public services are the last bastion of unionisation in Britain) see resisting change as their raison d'être. So the hardest part of the government's task is getting the unions to agree to change.

Mr Blair has made his task harder by committing a classic negotiating error. Instead of extracting concessions from the other side before promising his own, he has pledged himself to higher spending on public services without getting a commitment to change from the unions. In 2000, for instance, the government promised the health service a 6.1% average annual increase in the four years to 2003-04. Why, given that this pledge has been made, should the health unions give ground in return? In a speech on March 20th, Gordon Brown, the chancellor of the exchequer, said that “the something-for-nothing days are over in our public services and there can be no blank cheques.” But the government already seems to have given health workers a blank cheque.

Nor are other ministries conveying quite the same message as the Treasury. On March 19th, John Hutton, a health minister, announced that cleaners and catering staff in new privately-funded hospitals working for the National Health Service will still be government employees, entitled to the same pay and conditions as other health-service workers. Since one of the main ways in which the government hopes to reform the public sector is by using private providers, and since one of the main ways in which private providers are likely to be able to save money is by cutting labour costs, this move seems to undermine the government's strategy.

May the force be with them

Now the government faces its hardest fight. The police need reforming more than any other public service. Half of them, for instance, retire early, at a cost of £1 billion ($1.4 billion) a year to the taxpayer. In Merseyside, the figure is 77%. Their sick-leave levels are ludicrous, their overtime arrangements antediluvian. The police have voted 10-1 against proposals from the home secretary, David Blunkett, to reform their working practices. Last week they organised a mass protest outside Parliament, and chief constables all around the country are bending the ears of all the big-wigs they know. Mr Blunkett sounds determined—“I have powers to push through reforms about the way the force is managed and I will do that,” he says—but the power of the police lobby has defeated previous attempts at reform.

This is a fight the government has to win. If the police get away with it, other public-service workers will reckon they can too. And, if they all get away with it, Mr Blair's domestic policy—which is what voters are most likely to judge him on at the next election—will be a failure.

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About sponsorship

European bankruptcies

Fear of failure

Mar 21st 2002
From The Economist print edition

The best way to help European firms is to make it easier for them to fail

EUROPE is desperate to succeed in business. Two years ago, the European Union's Lisbon summit set a goal of becoming the world's leading economy by 2010. But success, as any new-age executive coach might tell you, requires confronting the fear of failure. That is why Europe's approach to bankruptcy urgently needs reform.

In Europe, as in the United States, many heavily indebted companies are shutting up shop just as the economy begins to recover. The cull will be worst in telecoms and technology but is also sweeping through other industries. Ironically, the upturn is often the moment when weak firms finally fail. But America's failures have a big advantage over Europe's weaklings: their country's more relaxed approach to bankruptcy.

In the United States, the Chapter 11 law makes going bust an orderly and even routine process. Firms in trouble simply apply for breathing space from creditors. Managers submit a plan of reorganisation to a judge, and creditors decide whether to give it a go or to come up with one of their own. Creditors have a say in whether to keep the firm running, or to liquidate it. If they keep it running, they often end up with a big chunk of equity, if not outright control. So ordinary has this become that such “restructurings” are now almost as common as flotations were in the boom days.

In Europe, by contrast, failed firms face bigger hurdles (see article). First, in the continent that created the debtor's prison, insolvency is still tainted with moral failure. In some countries, company directors are personally liable for bankruptcy. That steeply raises the penalties for failure—and so deters entrepreneurs from taking risks.

But shutting a bust European company is harder in two other ways. First, with no equivalent of Chapter 11, bankruptcy forces companies to stop trading abruptly. That damages the value of the creditors' potential assets, and may also cause havoc for customers. When Swissair ran out of money last year, it had immediately to stop flying. Second, a company that trades across the European Union will find that it has to abide by different bankruptcy laws in the 15 member states, whose courts and administrators may make conflicting and sometimes incompatible stipulations.

The absence of provision for negotiations between companies and creditors increases the temptation for government to step in. Two years ago Holzmann, a German construction firm, was rescued by the government. Now it is in trouble again, and the government has leaned on big German banks to bail it out. In France Bull, the national information-technology champion, is about to receive yet more state aid to stave off failure. When governments do not come to the rescue, the lack of clear rules can lead to chaos. Kirch, a big German media group, is mired in a swamp of creditor negotiations. As a result of all this, Europe's teetering firms miss the chance to become more competitive by selling assets to others who might manage them more efficiently. Their sickly American rivals survive, transformed, to sweep the field.

An opportunity now exists to think again about Europe's approach to bankruptcy. The European Union is expected to issue a new directive on the subject in May. Germany has begun to update its insolvency law. And last year Britain produced a white paper saying that a rigid approach to bankruptcy could stifle the growth needed to meet Lisbon's goals.

At the 11th hour

So why not a Europe-wide Chapter 11? Europe's politicians instinctively mistrust America's law, seeing it as a cosy convalescent home for sick companies. Certainly this has been true in some celebrated cases. Eastern Airlines continued to fly long after it should have been put out of its misery; TWA went bust three separate times (wags called these Chapter 11, 22, and 33), while rival American Airlines complained mightily about this unfair competition. Today, European telecoms companies say much the same about their bankrupt, yet still-trading, American competitors. Moreover, critics say, managers too often keep their jobs (or, as at Enron and Polaroid, take hefty “retention bonuses”) while shareholders walk away empty-handed. But these problems could be avoided in a European version of the law.

At present, Europe's approach offers retribution for the disgrace of letting lenders down. That may be just, but it is the wrong way to build value and to create a truly common market for companies. Failure, like success, calls for a common approach in Europe.

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Letters

Mar 21st 2002
From The Economist print edition

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Teachers v vouchers

SIR – It is no surprise that *The Economist* supports school vouchers despite the fact that vouchers have no record of success and divert scarce resources from the public schools that educate 90% of American children ("Hands up for vouchers", February 23rd). It is a surprise, however, that you claim that teachers' unions "do not really dispute the idea that voucher children can get a better education in faith-based schools."

No independent research has showed that vouchers are effective. The official state-mandated study of the Cleveland voucher programme, for instance, tested students in language, reading and maths over two years and found that the gains of public-school students were greater than those of voucher students. The study also found that "student academic achievement...presented no clear or consistent pattern that can be attributable to [voucher] programme participation."

Teachers support measures that have proved effective in turning around low-performing schools, such as smaller classes, research-backed instructional methods, quality professional development for teachers, high academic standards and extra help for students who struggle to meet those standards. Many urban schools have instituted these reforms and are seeing a significant rise in student achievement.

This is not to say that there are not problems in many of our urban public schools. The learning gap between the affluent and the less well off is too great. But the only proven way to close the gap is by investing in research-backed programmes, not by offering the false hope of vouchers, which provide for only a small number of families and take more money away from already underfunded urban schools.

Sandra Feldman
President
American Federation of Teachers
Washington, DC

State assemblies

SIR – In considering a name for a new German state combining Berlin and Brandenburg, you call Berlin-Brandenburg "cumbersome and ugly" ("Prussian blues", March 2nd). In a nation that includes Mecklenburg-Vorpommern, Schleswig-Holstein, Sachsen-Anhalt, Nordrhein-Westfalen, Rheinland-Pfalz and Baden-Württemberg, who could object to the relatively poetic (and pronounceable) Berlin-Brandenburg?

Matt Simon
Boston

Manufacturing fairness

SIR – You are right that manufacturing is no more special than any other sector of the economy ("Does it matter?", March 9th). However, the Engineering Employers' Federation (EEF) argues that it should receive fair treatment. This would include policies to encourage investment in skills and research and development, and avoiding discriminatory policies like the climate-change levy which overly penalises manufacturing and removes money that could be invested in energy-efficiency technologies. As well as

boosting trade, productivity and innovation, a stronger manufacturing sector would contribute to a more balanced regional economy, reducing strains on the housing market and public services in London and the South-East. This is surely something we could all agree on.

Stephen Radley
EEF
London

Canada's nasty neighbour

SIR – Your Eurocentric version of the universe only recognises America's trade-bullying tactics when they affect you ("George Bush, protectionist", March 9th). Poor old Canada, with a free trade pact no less, has been subjected to these tactics time and time again. The most pressing problem at the moment is the soft-wood lumber dispute, an issue that has been with us for over 100 years. Despite many rulings in our favour over many years, our lumber industry is still at America's mercy. America's only interest is denying access for our wood to its market, despite the fact that most experts agree that harvestable timber is running out there.

You regard Canada as a dull, boring place, fit only for lumberjacks and trappers, but we live next door to the United States and often bear the brunt of its policies much before you do.

Gary Moore
Delta, Canada

Containing terrorism

SIR – Your article on containers makes several statements that are flatly untrue ("The Trojan box", February 9th). The container-security strategy I proposed will prevent and deter the use of ocean-going cargo containers for concealing terrorist weapons by screening containers at the port of origin, before they are shipped. My strategy calls for a security standard to which all major trading nations agree. Nations would target and screen departing containers using their own officers. The United States Customs Service would station officers at foreign ports to work beside officers of the host nation and assist them with targeting and examining containers when necessary.

My strategy would not limit trade to the ten top ports. I propose only that we start with the top ten, as half of all containerised freight destined for America arrives from these ports. Any nation that sees common security standards as in its own self-interest is welcome to join this effort. The strategy is not just in America's interest, but in the interest of every nation with an economy dependent on trade moved by container ships.

Robert Bonner
Commissioner
US Customs Service
Washington, DC

Sitting target

SIR – Maybe, as you report, guns were more common than chairs in some parts of America in the late 18th century ("Just another piece of furniture", March 9th). And you can be sure that if we now had a coalition of liberals and foreign newspapers trying to take away our chairs, America's National Chair Association would prove both strong and combative.

Jose Rodriguez
Houston

South America's success

SIR – In your analysis of Latin America's situation you mention two exceptions to the current turmoil, Mexico and Brazil, but miss the most prominent ("Losing its way?", March 2nd). Chile has shown a steady average growth of 6% in the past 18 years. It has almost no inflation, an open market with trade accounting for about 50% of its GDP and institutions that work about as well as in developed countries. People pay taxes and respect the law. Basic social indicators such us life expectancy, mortality rate, and

water and electricity availability rank alongside countries with twice the income per person.

Chile shows that it is possible to defeat the Latin American curse by adopting an open market and political reform accompanied by the political courage to implement second-tier reforms in pensions, education and health. Chile has a long way to go but its past accomplishments deserve a mention.

Rafael Rodriguez
Santiago

SIR – You imply that Latin America's politicians and citizens have misplaced blame, singling out a political straw man rather than the real causes of the problem. Yet the changes in the region—reduced protectionism, increased foreign investment and open markets—were achieved through concrete policies that incurred the painful social costs of unemployment and falling wages, even as they purported to deliver new opportunities. Today's bitter protests are not knee-jerk attacks on a trumped up scapegoat but the legacy of sacrifice, hard work and a hope unfulfilled.

Rudi Colloredo-Mansfeld
Iowa City

Gospel truth

SIR –“The spirit is willing but the flesh is weak” may be a “famous Russian saying” as you inform us (“Tongues of the web”, March 16th), but surely the copyright belongs to Jesus Christ or to His chronicler, St Matthew (Chapter 26, verse 41).

Marques de Tamaron
London

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George Bush and Latin America

But does he really love her?

Mar 21st 2002 | WASHINGTON, DC
From The Economist print edition

The president is only partly redeeming his pledge to make Latin America "a fundamental commitment of my presidency"

THIS week, George Bush makes his first trip to Latin America since September 11th. It will be a test of his new policy towards the continent. It is also a test of whether "second order" foreign-policy issues really matter to the president now.

In a campaign speech in Miami in August 2000, Mr Bush promised a big change in his country's approach. "Latin America", he said, "often remains an afterthought of American foreign policy." As president, he would "look south, not as an afterthought, but as a fundamental commitment."

In his first months in office, Mr Bush tried hard. He met a stream of Latin American leaders. He threw his support behind the mooted Free Trade of the Americas Agreement at a summit in Quebec City. Finally, he devoted his first (and so far only) state dinner to the president of Mexico, Vicente Fox, where he proclaimed Mexico to be "our most important relationship".

That was on September 6th. Five days later, Latin America became the invisible continent again. Few could blame the administration for concentrating on other things. But American policy towards Latin America has long been notorious for being easily distracted. Little has changed.

When Argentina imploded in December, the White House stood by and let events take their course. Mr Bush took a year to appoint the State Department official responsible for the region. He even failed to get the Senate to renew a law giving drugs-producing Andean countries tariff breaks on products that offer an alternative to narco-business. To many in the region, these signs of neglect were all the more worrying because they occurred just when political upheaval was breaking out from Buenos Aires to Caracas, when growth and investment were collapsing, and when the continent again seemed threatened by populism. No wonder Latin leaders worry that candidate Bush's promises may turn out to be hot air.

Mr Bush's trip to Mexico, El Salvador and Peru is designed to reassure people—both in the region and in the United States, with its millions of Latino voters—that Latin America still matters. Of course we are engaged, his officials claim. Look at trade: we are busy at the continental level (the FTAA); the regional one (Mr Bush is talking about a new Central American free-trade area) and bilaterally (a US-Chile trade agreement should be ready in May). What nonsense to suggest otherwise.

The trouble is that in trade and in three of the continent's most important

In three of the

countries—Mexico, Colombia and Argentina—Mr Bush is arriving fairly empty-handed. Take Mexico. Mr Bush will attend the aid conference in Monterrey hosted by Mr Fox, a friendly gesture (see article). He will also set up a $30m aid fund to encourage investment in the poor south of Mexico (the bit that has not benefited from NAFTA). But this has little to do with the main business between Mexico and America, which is immigration. Mr Fox wants America to institute some sort of amnesty or legalisation programme for the 3m Mexicans working illegally in the United States. American employers would like a new temporary-worker programme to make it easier to hire Mexican workers. Neither of these things will happen in the wake of September 11th.

continent's most important countries, Mr Bush is arriving empty-handed

That does not mean nothing is going on. Earlier this month, Congress passed a law making it easier for Mexicans in the United States to get permanent residency (the law, known as the 245i provision, means they no longer have to leave the country while they wait for a green card, a process than can take years). Mexico and America will also sign an agreement to spruce up the policing of their border. But all that is a far cry from the “grand bargain” Mr Fox had hoped for.

Or take Argentina, a country Mr Bush was planning to visit until last year's chaos. There is no real American policy towards the region's third-largest economy. Mr Bush is not booked to meet Eduardo Duhalde, the Argentine president, in Monterrey. No one in the administration is sure what the Duhalde government's economic plans actually are, or even whether it will survive. So policy has been subcontracted to the IMF, where it is treated (naturally) as a technical, economic matter.

Only in Colombia are there signs of greater involvement. America gives Colombia around $1 billion a year in military aid. This is supposed to be spent only on programmes to eradicate drugs. Last year, as violence increased between the government and the FARC, President Andres Pastrana asked Mr Bush if he could use American equipment in his fight against the guerrillas. Mr Bush refused.

That is now changing. Last week, for the first time, the under-secretary of state for the western hemisphere, Otto Reich, referred to the FARC as “terrorists” not “guerrillas”. As *The Economist* went to press, the administration was preparing to ask Congress for a new aid package allowing the Colombian government to use American military kit for counter-insurgency.

Which leaves trade—for most Latin American countries, the most important matter. Mr Bush's commitment to free trade in the Americas seems genuine. He also has a strategy for getting there: the idea is to push for trade agreements on all fronts, bilaterally and regionally, creating a competition of liberalisation.

But domestic politics gets in the way. Mr Bush has not got Trade Promotion Authority (TPA), the negotiating power that is essential to conclude big trade deals. Although it narrowly passed the House of Representatives in December, TPA is stuck in the Senate, mired in arguments about helping workers who have lost their jobs because of imports. Worse, the TPA bill that the House passed carries the stamp of Florida's citrus farmers: it blocks freer trade in agricultural products, notably orange juice, to Brazil's especial dismay.

Even more embarrassing, Mr Bush will discuss trade with ministers from Andean countries just after they have lost their special trade preferences from America. The Andean Trade Preferences Act expired in December 2001 and, although the Bush administration announced a one-off 90-day suspension of tariffs in February, there is still no replacement, largely because America's textile lobby is holding it up. Worse, as part of the deal to pass TPA, House Republicans promised not to pass any new trade laws without revising an existing deal with the Caribbean. So the Andean mess will not be sorted out before the summer. And the recent steel tariffs (minimised in so far as they applied to Latin America) have also added to scepticism about Mr Bush's ability, or eagerness, to achieve free trade.

All the same, the best reason for thinking America will one day forge a new relationship with its southern neighbours is Mr Bush himself. He is probably the most forceful advocate of a new policy in his own administration, partly because of his background as governor of Texas, partly because he is more sensitive to the nuances of domestic politics than the cold-warrior types in his foreign-policy team. But if the current trip is anything to go by, engaging anew is something even the president cannot do without huge effort.

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Immigration

Inept National Security

Mar 21st 2002 | LOS ANGELES
From The Economist print edition

Upset with the INS? How about merging it with Customs?

Get article background

AP

About to get married

"WORSE than useless," fumed Darrell Issa, a Republican congressman from California, on March 19th, when the House Judiciary Committee held a hearing on the Immigration and Naturalisation Service. "Terrible, and getting worse," added Zoe Lofgren, a Democratic colleague who has kept a watchful eye on the INS for ten years.

The previous week, six months to the day after terrorists had attacked America, a flying school in Florida had received word from the INS that it had issued visas allowing Mohamed Atta and Marwan al-Shehhi to enrol there as students. Atta and al-Shehhi, who had taken their flying lessons over a year earlier, are believed to have been piloting the airliners that hit the twin towers in New York. This did not make the agency look good.

Committee members therefore lined up to take swings at James Ziglar, the head of the INS. He explained, somewhat pathetically, that "outdated procedures" had kept the visa-processing wheels grinding slowly through a backlog of applications. These had now been scrapped.

He also had some new rules in mind to tighten up visas. No longer would visitors arriving in America on a tourist visa be able to switch to a student visa once in the country and so extend their stay. Nor would foreigners be allowed to start studying until their visas had been approved. Tourist visas would last for 30 days rather than six months.

Speeding up the paperwork—and getting more of it on to computers—is vital, but September 11th has raised larger questions about the INS. Above all, the September attacks have exposed the tension between the agency's two jobs: on the one hand enforcing the security of America's borders, and on the other granting privileges such as work permits to foreigners.

Businesses wanting to employ talented foreigners, such as the high-tech firms of Silicon Valley where Ms Lofgren has her seat, want smoother, quicker service from the INS. But when money and staff are short, as they have been in the past, speed comes at the expense of scrutiny. More money could help: the administration's budget proposal included an increase of 13% in the agency's funding, from $5.6 billion this year to $6.3 billion next, and will add 1,800 to its staff of 35,000. But other people want more radical changes.

James Sensenbrenner, a Republican congressman from Wisconsin, wants to split the INS into two separate bodies, one dealing with border security and the other with handling benefits to immigrants. The other approach, favoured in the White House, is to treat the two functions as complementary, and to give the INS even more responsibility for security. Under that plan, the INS would merge with the Customs Service, which monitors the 20m shipments of goods brought into America every year, as well as the bags carried in by some 500m visitors. The two agencies would form one large body within the Department of Justice, the current home of the INS. This would cut out some of the duplicated effort at borders, where customs officers and agents from the INS's Border Patrol often rub shoulders but do not work together.

Mr Bush—who has said that the news of the visa approvals left him "plenty hot"—was expected to give

his approval as *The Economist* went to press. The Senate, however, may not be quite so keen. The Justice Department could have trouble handling such a merger, let alone taking on the considerable economic responsibilities of the Customs Service, which is currently part of the Treasury.

The Senate prefers yet another set of security recommendations, including links between the databases of different agencies that hold security and immigration information, and scanners at ports of entry to check biometric data recorded on immigration documents. These ideas are embodied in a bill sponsored by members of both parties, but are currently held up by Robert Byrd, the chairman of the Senate Appropriations Committee, who worries that there has not been enough debate on the subject. Mr Ziglar, poor chap, may feel there has been more than enough.

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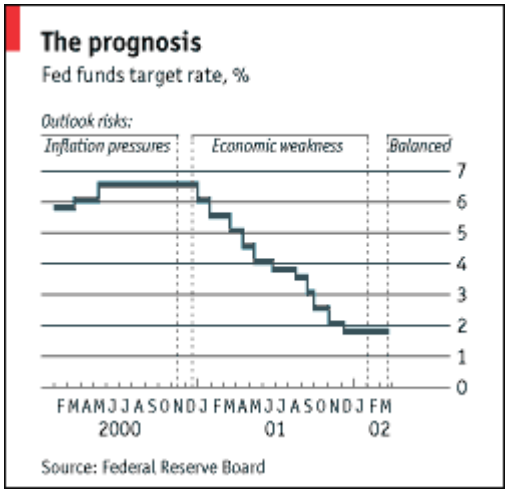
The economy

When will interest rates rise?

Mar 21st 2002 | WASHINGTON, DC
From The Economist print edition

Maybe not quite as soon as the market expects



AMERICA'S central bank sent a clear message this week. For the second consecutive meeting, the Federal Open Market Committee, the central bank's policy-making committee, left short-term interest rates unchanged at 1.75%. But it said that the risks facing the economy had shifted from economic weakness to a balance between weakness and excessive growth. This shift surprised no one. But it has convinced many people that interest rates are set to rise again—and soon.

Judging by prices in futures markets, investors are betting that short-term interest rates could start rising as early as May, and will be 1.25 percentage points higher by the end of the year. That may be excessive. Economists at Goldman Sachs, who long argued that the central bank would do nothing this year, now expect short-term rates to go up only 0.75% this year, starting in June. But virtually everyone reckons some Fed tightening is in the offing.

The reason? After an unprecedented 11 rate-cuts in 2001, short-term interest rates are abnormally low. As the signs of robust recovery multiply, analysts expect the Fed to take back some of the rate cuts it used as an “insurance policy” after the September 11th terrorist attack. They think there will be a gradual move from the Fed's current “accommodative” monetary stance to a more neutral policy. And a neutral policy, many argue, ultimately implies short-term interest rates of around 4%.

Logical enough. But higher rates could still be further off, particularly if the recovery proves less robust than many hope. Certainly, recent economic indicators have been extraordinarily strong: unemployment fell for the second consecutive month in February and industrial production rose in both January and February. The manufacturing sector is growing after 18 months of decline. The most optimistic Wall Streeters now expect GDP to have expanded by between 5% and 6% on an annual basis in the first quarter.

But one strong quarter does not imply a sustainable recovery. In the short term, the bounce-back is being driven by a dramatic restocking of inventories. But it can be sustained only if corporate investment recovers and consumer spending stays buoyant. With plenty of slack capacity around and many firms stuck with huge debts and lousy profits, it is hard to see where surging investment will come from. And, despite falling unemployment, America's consumers could disappoint the bulls. They face higher energy prices. The quick route to cash through mortgage refinancing is closing off. And since consumer spending held up so well during the “recession” it is unlikely to jump now.

These uncertainties alone suggest the central bank will be cautious about raising interest rates. That caution is all the more necessary given the lack of inflationary pressure. Although America's consumer prices have stopped falling on a monthly basis, the latest figures show few signs of nascent price pressure. Indeed, given the huge pressure on corporate profits, the Federal Reserve might be happy to see consumer prices rise slightly. In short, while Wall Street frets about when and how much interest rates will go up, the answer may well be not soon and not much.

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Atlanta's traffic

In King Roy's snarled domain

Mar 21st 2002 | ATLANTA
From The Economist print edition

Forget buses and trains; just build more highways, dammit

AP

AFTER Los Angeles, Atlanta may be America's most car-dependent city. Atlantans sentimentally give their cars names, compare speeding tickets and jealously guard any side-street where it is possible to park. The city's roads are so well worn that the first act of the new mayor, Shirley Franklin, was to start repairing potholes. In 1998, 13 metro counties lost federal highway funds because their air-pollution levels violated the Clean Air Act. The American Highway Users Alliance ranked three Atlanta interchanges among the 18 worst bottlenecks in the country.

Other cities in the same fix have expanded their public-transport systems, imposed commuter and car taxes, or reorganised their highways. Atlanta does not like any of these things. A vast public-works project such as Boston's Big Dig would be booed in a city that turned almost exclusively to private money for the 1996 Olympics. (Come to that, Bostonians, after years of Big-Dig-induced snarls, are not mad keen on it either.) In last year's mayoral election in Atlanta, only the least popular candidate dared mention a commuter tax. Ms Franklin pooh-poohs the idea.

Public transport is a vexed subject, too. Atlanta's metropolitan region is divided into numerous county and smaller city governments, which find it hard to work together. When the Metropolitan Regional Transit Authority (MARTA), the local light-rail-and-bus system, was proposed in 1971, only two counties, Fulton and DeKalb, agreed to finance it. Clayton, Gwinnett and Cobb, moved by a mixture of racism and a wish for a quiet life, refused, and MARTA has been unable to expand.

Railways now serve the city centre and the airport, but not much else; bus stops are often near-invisible poles, three feet high, offering no indication of which bus might stop there, or when. A one-way fare is $1.75, compared with $1.50 in New York, yet in 1999 MARTA collected only 26% of its revenue from fares, whereas New York collected 64%. Over loud protests, the system recently solved an $8m deficit by cutting bus routes and raising fares.

Georgia's Democratic governor, Roy Barnes, who hopes for re-election in November, has other plans. To win back the federal highway money lost under the Clean Air Act, he created the Georgia Regional Transportation Authority (GRTA), a 15-member board with the power to make the county governments, the city and the ten-county Atlanta Regional Commission co-operate on transport plans, whether they like it or not. Last year, when Mr Barnes announced his $8.3 billion plan, he entrusted GRTA with the money.

Now GRTA has issued its own preliminary plan, allocating $4.5 billion over the next three years for a variety of schemes. The plan earmarks money to widen roads; to have an electric shuttle bus shuttle tourists among the elegant villas of Buckhead; and to create a commuter rail link between Atlanta and Macon, two hours to the south. Counties will be encouraged, with generous ten-to-one matching funds, to start express bus services.

GRTA has notched up some successes. Its first substantial programme, a bus service in Clayton County, began in November 2001 and now serves 1,400 riders every weekday, roughly twice as many as the planners expected. Gwinnett County also introduced a bus service in 2001; before it did so, it was the largest county in the United States without any form of public transport.

Public goodwill, however, may not stretch as far as the next plan, which is to build the Northern Arc highway for 65 miles across three counties north of the city limits. GRTA has allotted $270m for this. Supporters say it would ease the congestion on local roads; opponents think it would worsen over-development and traffic. The counties affected, and even GRTA's own board, are divided.

The governor is in favour, however; and since he can appoint and fire GRTA's members, that is probably the end of the story. Mr Barnes has a tendency to do as he wants, regardless. His opponents started calling him “King Roy” after he pushed a new state flag, downplaying unacceptable Confederate symbols, through last year's state legislature without a popular vote. His arrogance on traffic matters could also lose him votes. But Mr Barnes think that Atlanta's slowing economy (in 2001 only New York city lost more jobs) could do him more harm than the anti-sprawl movement. And, in the words of a former state attorney-general, “Most people don't give a rat's behind about sprawl. They don't want to sit in traffic.”

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Telemarketing and politics

“Honey, George Bush is on the line”

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Politicians can now phone millions of voters. Unfortunately

AP

Am I bothering you?

A TYPICAL evening in Chicago. First the mayor, Richard Daley, rings up to speak about the Illinois Democratic primary on March 19th. Not long after that, Senator Richard Durbin and former Senator Paul Simon both phone to give their thoughts. Then Gloria Steinem calls to mention how much she likes the Republican candidate for governor.

Has your correspondent become a power-broker in Illinois politics? Well, yes, of course. But he is also the victim of a relatively new technology that marries the worst two nightmares of any soul who wants to eat supper in peace: windy politicians and telemarketing.

Voice-broadcasting technology now enables a politician to record a message, which may be anything from a few seconds to several minutes long, on to a computer, load the phone numbers of the voters to be targeted, and then “blast” the message to some 140,000 phone numbers at a time, or millions of households a day. Officials at one blaster firm, Xpedite, reckon that it costs eight cents a call for its “voice-reach” service to connect politicians with voters, compared with 35 cents for a live telemarketer to make the call.

Does it sway voters? Politicians seem to think so. The technology first reared its ugly head in tightly contested areas of the 2000 presidential race. (John McCain was the victim of a particularly nasty and effective blasting campaign by unofficial supporters of the current president.) Since then, Xpedite says it has done work for candidates in more than 45 states. The firm is almost fully booked for the November elections.

Politicians are not the only ones who want to blast their thoughts into phone-owners' ears. Businesses can deliver urgent news to customers; stockbrokers can give clients hot tips; schools can tell parents their kids didn't turn up, or that school is shut; cities can tell people that a storm is on its way. Supper in America will never be the same, now that George Bush may ring up at any moment.

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Medical malpractice

The wrong sort of clinical trials

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From The Economist print edition

A new law in Pennsylvania may leave doctors a little better protected

WHEN it comes to suing doctors, Philadelphia is hardly the city of brotherly love. A combination of sprightly lawyers and sympathetic juries has made Philadelphia a hotspot for medical-malpractice lawsuits. Since 1995, Pennsylvania state courts have awarded an average of $2m in such cases, according to Jury Verdict Research, a survey firm. Some medical specialists have seen their malpractice insurance premiums nearly double over the past year. Obstetricians are now paying up to $104,000 a year to protect themselves.

Pennsylvania's predicament is severe, but not unique. At least 35 other states, notably Florida and Nevada, have experienced sharp rises in medical malpractice insurance rates since 2000. According to *Medical Liability Monitor*, some doctors, such as general surgeons, face median rate hikes of 15% this year.

The insurance industry is largely to blame. Carol Golin, the *Monitor*'s editor, argues that in the 1990s insurers tried to grab market share by offering artificially low rates (betting that any losses would be covered by gains on their investments). The stockmarket correction, coupled with the large legal awards, has eroded the insurers' reserves. Three in Pennsylvania alone have gone bust. At the end of last year, the St Paul Companies, an insurer which had provided one in ten medical malpractice policies, announced it was getting out of that business, leaving 42,000 doctors to find alternatives.

In the 1970s and 1980s, doctors were able to pass on big rate hikes to their patients. This time, points out William Sage, a law professor at Columbia University, “managed care” regimes set limits on what doctors can charge.

A few doctors—particularly older ones—will quit. The rest are adapting. Some are abandoning litigation-prone procedures, such as delivering babies. Others are moving parts of their practice to neighbouring states where insurance rates are lower. Some from Pennsylvania have opened offices in New Jersey. New doctors may also be deterred from setting up shop in litigation havens, however prestigious.

Despite a Republican president, tort reform has got nowhere at the federal level. Indeed doctors could get clobbered indirectly by a Patients' Bill of Rights, which would further expose managed care companies to lawsuits. This prospect has fuelled interest among doctors in Pennsylvania's new medical malpractice reform bill, which was signed into law on March 20th. It will, among other things, give doctors $40m of state funds to offset their insurance premiums, spread the payment of awards out over time and prohibit individuals from double-dipping—that is, suing a doctor for damages that have already been paid by their health insurer.

But will it really help? Randall Bovbjerg, a health policy expert at the Urban Institute, argues that the only proper way to slow down the litigation machine would be to limit the compensation for pain and suffering, so-called “non-monetary damages”. Needless to say, a fixed cap on such awards is resisted by most trial lawyers. But Mr Bovbjerg reckons a more nuanced approach, with a sliding scale of payments based on well-defined measures of injury, is a better way forward. In the meantime, doctors and insurers are bracing themselves for a couple more rough years before the insurance cycle turns.

Nobody disputes that hospital staff make mistakes: a 1999 Institute of Medicine report claimed that errors kill at least 44,000 patients a year. But there is little evidence that malpractice lawsuits on their own will solve the problem.

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Justice for Indians

A long-overdue scalping

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A plaintiff from the Blackfeet may have the courts going her way

AP

Cobell gathers her troops

IF THE opinion polls are to be believed, most Americans are coming to trust their government more than they used to. The habit has not yet spread widely among American Indians, who suspect an organisation which has so often patronised them, lied to them and defrauded them. But the Indians may soon win a victory in a legal battle that epitomises those abuses.

Elouise Cobell, a banker who also happens to be a member of the Blackfeet tribe in Montana, is the leading plaintiff in a massive class-action suit against the government. At issue is up to $10 billion in trust payments owed to some 500,000 Indians. The suit was filed by Ms Cobell back in 1996; she now has more than 300,000 joint plaintiffs from dozens of tribes.

The suit revolves around Individual Indian Money (IIM) accounts that are administered by the Interior Department's Bureau of Indian Affairs (BIA). Back in the 1880s, the government divided more than 11m acres of tribal land into parcels of 80 to 160 acres that were assigned to individual Indians. Because these parcels were rarely occupied by their new owners, the government assumed responsibility for managing them. As the Indians' trustee, it leased the land out for grazing, logging, mining and oil drilling—but it was supposed to distribute the royalties to the Indian owners.

In fact, officials admit that royalties have been lost or stolen. In some cases the money was never collected in the first place. Records were destroyed, and the government lost track of which Indians owned what land. The plaintiffs say that money is owing to 500,000 Indians, but even the government accepts a figure of about 300,000.

Ms Cobell and her seven siblings grew up in a one-bedroom house on the Blackfeet reservation without electricity, telephones or running water. For years, she heard Indians complain of not getting payment from the government for the oil-drilling and ranching leases on their land. So, after she had been to college and become treasurer of the Blackfeet nation in the late 1970s, she asked BIA officials what was going on. They told her she had misread the numbers. In 1994 she and other tribal leaders successfully pushed for the creation of a special trustee for the funds. But nothing much got done. Ms Cobell returned to Washington and, after a brush-off from government lawyers, filed the suit.

Since then, the courts have gone her way. “I've never seen more egregious misconduct by the federal

government," said Royce Lamberth, a federal district judge, in 1999, fining the interior secretary, Bruce Babbitt, and the treasury secretary, Robert Rubin, more than $600,000 for failing to disclose the destruction of documents relating to the case. The same judge ruled that the government had breached its responsibilities to the Indians, and said the trust fund would remain under court jurisdiction for at least five years. An appeal against the ruling was denied last year.

Over to Gale Norton, George Bush's interior secretary. She was charged with contempt in November because her department had failed to fix the problem. In December, Judge Lamberth ordered the Interior Department to shut down all its computers for ten weeks because trust-fund records were vulnerable to hackers. The system was partly restored last month and payments to some Indians, which had been interrupted, resumed. But tens of thousands of Indians, it seems, are still waiting for their cheques.

Judge Lamberth's ruling in Ms Norton's contempt trial is expected soon. If the judge finds that she wilfully misled him, he could fine her and, in theory, send her to prison. Later this year the court will tackle the question of deciding how much money is owed to Indian beneficiaries of the trust accounts.

And that is not the end of it. Ms Norton has proposed the creation of a new Bureau of Indian Trust Management, separate from the BIA. Indians are cross that she suggested this without consulting them. Some want the trust funds to be placed in receivership, under a neutral supervisor. Others have called for Congress to establish an independent commission, including Indians, to draw up a plan for reforming the whole system. A messy injustice may at last be getting sorted out.

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Lexington

The faith of the fathers

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The Catholic church's deepest challenge may not be paedophilia, but the withering of its cultural roots

THE archdiocese of Boston has given the police the names of over 80 priests suspected of sexual abuse. Two consecutive bishops of Palm Beach have resigned because of their taste for young boys. Two priests, from Baltimore and St Louis, have been arrested as members of a child-pornography ring. All in all, some 2,000 priests stand accused of sexual abuse—the ultimate betrayal of the trust that is embodied in the word “father”.

The scandal is not just the number of offenders. It is also the church hierarchy's complicity in evil—its preference for shielding priests from disgrace, rather than protecting children. The Boston hierarchy spent 30 years moving one known paedophile from parish to parish, allowing him to prey on 130 young victims. Other dioceses have done the same, though on a lesser scale.

What has brought this disaster on the church? Left-wing Catholics say it is celibacy—a tradition that dissuades many normal men from joining the priesthood and puts huge pressure on those that do. Some conservatives are blaming “lavender priests”, arguing that many so-called paedophile cases involve adolescents rather than young children. But the church's current agonies stem not only from sexuality, but from social change. The Catholic church was once one of the most powerful forces in American life because it was rooted in a vigorous Catholic culture; the withering of that culture is weakening the church and rendering it vulnerable to all sorts of infections.

Catholic culture in the United States was the fruit of mass immigration, and Irish immigration in particular. The Irish who flooded into America from the 1840s onwards brought with them a particularly doctrinaire, evangelical form of Catholicism. They faced challenges from softer Catholic traditions, particularly the lackadaisical Italians. But they eventually pushed other immigrant groups into subscribing to their version of the faith.

As Charles Morris points out in “American Catholic: The Saints and Sinners who Built America's Most Powerful Church” (Random House, 1997), they were extraordinarily successful. The Catholic church in America became not just one of the fastest-growing churches in the West but also one of the most pious. Catholics ran big American cities (where most of them settled), dominated the trade-union movement and colonised the Democratic Party. Perhaps their greatest achievement was to create a Catholic state-within-a-state, with its own schools, hospitals and welfare services: a state that could both shield its members from the temptations of a materialistic society and provide them with security from life's hardships.

The church prospered mightily from this success, not least because the priesthood had the pick of the brightest Catholic boys. The lords of the church were some of the most powerful men in the country, property magnates and political bosses rolled into one. Yet after the first world war every cardinal was the son of a working man. Catholic priests enjoyed fellowship and security as well as plenty of social prestige. Hollywood films such as “On the Waterfront” idealised “superpadres”; Catholic publicists like Bishop Fulton Sheen bestrode prime-time television much as Jay Leno does today.

The perils of success

But there has been a serpent in this paradise: assimilation. As Catholics became richer and more successful, they abandoned the Catholic-soaked ghettos for the more secular suburbs. They also partook of the fruits of higher education (including secularism and cynicism) in large numbers. And as Catholics became more like ordinary Americans, they became more addicted to American individualism and less willing to accept the diktats of Rome, particularly on birth control and women priests.

By 1970, though the church still had plenty of priests and coffers well-filled by wealthy parishioners, it was collapsing from within. Inner-city schools were losing pupils. The nuns who ran much of the Catholic welfare state were in ever shorter supply. In particular, the growing shortage of recruits for the priesthood forced the church to lower its standards. Those who came forward were sometimes accepted without thorough examination; those who strayed were kept on at all costs. Recruits complained of the absence of the old tradition of camaraderie and benign supervision. Today two-thirds of America's parishes have only one priest. A church bureaucracy that once ran urban America cannot keep order in its own house.

There is no doubt that the current scandal will continue to explode. The church's decision to come clean will cause much pain, even as it begins to purge the institution. Public prosecutors have got the bit between their teeth. Victims (and a few opportunists) have been emboldened to come forward. The church cannot solve any of its deep-seated problems without a bruising debate about one of its fundamental traditions: that the best point of contact between man and God is a celibate male priesthood. On that point, the Vatican is at present immovable.

Yet there is one silver lining on the darkening horizon. The inner cities may have been emptied of the children of European immigrants, but they are filling up with new arrivals from Mexico and farther south—the largest Catholic immigration in American history. Gregory Rodriguez, of the New America Foundation, points out that the churches in the south-west and west are full to bursting-point. Los Angeles is the biggest Catholic diocese in the country, the New York of the new century. Walk through LA's barrios, and you see makeshift shrines and handpainted pictures of the Virgin; visit its churches, and you see a riot of colourful banners and statues.

The new Catholicism that is being forged in such places is very different from the kind that used to dominate America: more focused on hearth and home than on building institutions. But it is a vital and expanding force. Irish immigration created American Catholicism. Latino immigration could renew it.

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Politics in Peru

The pressure on Toledo

Mar 21st 2002 | LIMA
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AP

A restored democracy struggles to find its feet

Get article background

IT WAS the last thing Peru needed. On March 21st, just three days before George Bush was due to make a brief visit to Lima, a powerful car bomb exploded near the United States' embassy, killing at least eight people and injuring up to 40. The government was already looking shaky. Since taking office as Peru's president last July, Alejandro Toledo has been hailed abroad as the embodiment of a newly restored democracy, after a decade of authoritarian rule by Alberto Fujimori. At home, he has disappointed. Each week sees protests by citizens demanding jobs and handouts, or denouncing the government's policies or its predecessor's abuses.

The bomb may have been the work of the Shining Path, a once-powerful Maoist terrorist group crushed by Mr Fujimori a decade ago. Its remnants (perhaps 400 or so fighters in remote jungle areas) have recently shown signs of life.

Mr Bush's visit is his first to South America, an opportune sign of friendship for Mr Toledo, an economist and Peru's first elected ruler of Andean Indian descent. Mr Toledo's approval rating has plunged, from 59% in August to just 25%, while 65% disapprove of the president, according to Apoyo, a polling company.

His basic problem is to have promised too much, and, so far, to have delivered too little. He has not yet learnt how to seem presidential: he is unpunctual (even by Latin American standards), has a facility for mis-speaking that rivals that of Mr Bush, and keeps changing his mind.

His latest mistake was to say that he would buy a presidential helicopter, to whisk him around a large and mountainous country more safely. Opposition media and politicians pounced. They said the money should go to alleviate poverty, and questioned the lack of a proper tender.

For his supporters, this incident was an example of the way in which every minor presidential stumble is magnified by a malicious campaign by powerful enemies. That campaign is led by two television channels whose owners are either in jail or on the run for taking bribes from Vladimiro Montesinos, Mr Fujimori's imprisoned spymaster.

In fact, for all his slips, Mr Toledo has not made huge mistakes. He has appointed some honest and capable ministers. But cleaning up the mess bequeathed by Mr Fujimori was never going to be easy. It is made harder by Mr Toledo's administrative inexperience, and by his lack of a reliable majority in

Congress, which is flexing its muscles after a decade of submission to Mr Fujimori.

The government's political frailty risks causing problems for an economy which has been reviving since Mr Toledo took office. The economy expanded by 3.9% in January compared with the same month last year. There is also growing confidence in the sol, the local currency. Richard Webb, the president of the Central Bank, points out that for the first time in two decades, Peruvians are selling dollars (which make up 65% of the money supply) and buying soles. Last month foreign investors snapped up $500m of Peruvian sovereign bonds—the first such issue since 1928.

But delivering the jobs and wage rises that ordinary Peruvians clamour for requires both faster growth and structural reforms. Despite lower interest rates, private investment, which fell sharply in Mr Fujimori's later years, is expanding only modestly. In part, that is because the banks are still weighed down by bad loans after the collapse of a credit bubble. Mr Webb says that the banks are hindered by bankruptcy rules that are generous to debtors.

Mr Toledo's economy minister, Pedro Pablo Kuczynski, is a former Wall Street banker, committed to privatisations and market reforms. But those plans risk being derailed. Next week, a civic “strike” is planned in southern Peru against electricity privatisation. And Congress, in populist mood, is debating several measures that may deter investment. It has already passed a tax-amnesty law that will cost the government nearly $100m a year. That makes it tougher for Mr Kuczynski to meet the target for this year's fiscal deficit.

After Mr Fujimori's corrupt and centralised autocracy, Peru needs institutional reforms. The new government has made a start on cleaning up the police and the army. But a wider reform of the state is making little progress. And a hasty decision by Mr Toledo and his Congressional allies to introduce an election for new regional governments in November may backfire. There are no safeguards against regional fiscal irresponsibility. As Augusto Alvarez of Apoyo points out, many of the protests are organised by local politicians with their eye on becoming regional presidents or mayors.

Mr Toledo's hopes are pinned on wide-ranging talks with opposition parties aimed at seeking broad policy consensus. These are buying the government some time, but are unlikely to survive the local election campaign. None of the main opposition leaders wants to see Mr Toledo's term cut short. But nor do they seem to have much interest in helping make it a success. For Peru's democracy, that looks like a missed opportunity—especially if bombings are set to return.

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Violence in Colombia

Gunned down

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Threats against labour and the church

Reuters

Get article background

An archbishop pays the price of speaking out

TWO men pulled Valmore Lacarno off a bus last March and shot him in the head in front of his fellow workers. The gunmen also picked out Victor Hugo Orcasita, tying him up and throwing him into a truck. Mr Orcasita's tortured and bullet-ridden body was found hours later. The dead men were leaders of the trade union at La Loma, a large open-pit coal mine in northern Colombia owned by Drummond, an Alabama firm. They were just two victims of a steadily mounting massacre of trade-union leaders in Colombia. Last year, 177 unionists were killed, up from 128 in 2000 and 69 the year before.

Last week, in a desperate effort to prevent further killings, the two men's families and union colleagues filed suit against Drummond in a court in the United States, claiming that the firm conspired with the right-wing paramilitary vigilantes of the United Self-Defence Forces of Colombia (AUC) to have the men killed. Witnesses allege that vehicles driven by AUC members regularly visited the mine, sometimes refuelling there. Drummond denies any involvement in the killings.

The case, like a similar suit filed against Coca-Cola in Florida last year, highlights the campaign of terror against trade unionists, and other civilian leaders, in Colombia. Neither the AUC, nor their leftist guerrilla opponents, recognise non-combatant status. The paramilitaries claim that some unions harbour guerrilla supporters, whom they consider to be “military targets”. But in many cases, say political analysts, the AUC has murdered union activists with no guerrilla link.

A government programme to protect trade unionists and other civilian leaders cannot keep pace with rising demand, despite having its budget increased from $2m last year to $10m this year. After receiving death threats, Messrs Lacarano and Orcasita repeatedly asked for protection, but to no avail. “Until someone gets killed, they don't believe you,” said Francisco Jaramillo, the leader of the national mineworkers' federation.

According to Carmen Maria Lasso, the protection programme's co-ordinator, threats against trade unionists have risen sharply since President Andres Pastrana called off peace talks with FARC guerrillas last month. In the past two weeks, 150 new pleas for protection have reached Ms Lasso's desk.

The plight of trade unionists is not unique. Many journalists and academics have been killed or forced to flee. Some have been victims of the guerrillas, and some of the paramilitaries. A UN human-rights report this week referred to “grave, massive and systematic” abuses, many of them the result of collusion or active collaboration between the paramilitaries and members of the armed forces.

Not even the Catholic Church is immune. On March 19th, Colombian politicians joined priests and ordinary citizens at the funeral of Isaias Duarte, the archbishop of Cali, Colombia's third city, gunned down as he left a church after a service. The most senior cleric to be murdered in Colombia, Archbishop Duarte had spoken out strongly against guerrilla kidnappings. But he had also denounced corruption. He had complained that drug traffickers, many of whom have close links to the AUC, had financed several successful candidates in this month's congressional election. He had been due to meet a prosecutor to elaborate on those allegations. As so often in Colombia, uncertainty surrounds the identity of the killers.

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Brazil's trade policy

Steeling for a fight

Mar 21st 2002 | SAO PAULO
From The Economist print edition

A battle against protectionist instincts

EVEN before George Bush slapped tariffs of up to 30% on imported steel this month, Brazil wondered if there was much prospect of a fair deal from the proposed Free Trade Area of the Americas (FTAA). Now, it has further reason for doubt. “America talks constantly about free trade but when it comes to practice, it is protectionist,” according to Jose Serra, President Fernando Henrique Cardoso's preferred candidate to succeed him in an election this year. That view, widely held in Brazil, means the country approaches further trade opening with caution.

American officials point out that the kind of steel that Brazil mainly exports to the United States (semi-finished slabs) will be unaffected by the tariffs. But Sergio Amaral, Brazil's trade minister, reckons the country could lose $80m a year in exports of other steel products. Add in a new farm bill, which proposes to give billions more in subsidies to American farmers, and Brazilian diplomats reckon it is hard to see an FTAA being worth very much.

Like the United States, Brazil has a government of many free-traders constrained by a sceptical Congress. Many legislators believe that Brazil opened its markets too widely in the early 1990s, and received too little access to other countries' markets in return. Such doubts were intensified by big trade deficits, as economic growth sucked in imports, especially from the United States. Only last year, following a forced devaluation of the currency in 1999, did Brazil's trade move into surplus (see chart).

Brazil remains quite protectionist, especially over products such as car parts and industrial machinery. The government also gives handouts to farmers, in the form of cheap credit, though it is far less generous than America's. And it disputes an American claim that its average tariffs are higher than those of the United States. America charges an average tariff of 46% on Brazil's top 15 exports to the world as a whole, whereas Brazil's average tariff on their American equivalents is just 14%, according to Rubens Barbosa, Brazil's ambassador in Washington. Fed up with this, Brazil has opened cases at the WTO against American barriers to its orange juice, its subsidies to soya and cotton growers, and now, too, its steel tariffs.

As well as the FTAA talks, Brazil and its partners in Mercosur (Argentina, Uruguay and Paraguay) are also holding free-trade talks with the European Union. So far, these talks have been modest, but Mr Amaral says that he and Pascal Lamy, the EU's trade commissioner, agreed recently that their scope should be broadened to include agriculture. Even so, Brazil's battle against farm protectionism is likeliest to bear fruit in the new round of WTO talks.

All three sets of talks are supposed to conclude in 2005. Those for the FTAA are most advanced. But Brazil's strategy for these talks has hit problems. It had dreamed of leading a common South American front to extract better terms from the United States. But many of its neighbours are keener to sign up for any half-decent trade offer.

So far, debate over the FTAA in Brazil has focused on protected industries which might at first lose out. But Brazil has many competitive products, from soybeans to shoes, whose exports should boom. And

new trade accords could draw in new foreign investment. Mr Amaral has ordered detailed studies of the impact of an FTAA. It is a sign of past caution that few such studies exist.

Brazilian officials say that before opening their markets further, they must reform taxes and cut the cost of credit. But they also know that Brazil must increase its exports, if it is to achieve faster growth and reassure investors that its foreign debt is manageable. If Mr Serra wins the presidential election, and whatever his doubts about American inconsistency, he is likely to sign up for an FTAA—even a less than perfect one, provided that, on balance, going in is better than staying out.

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Politics in Canada

Fresh faces

Mar 21st 2002 | OTTAWA
From The Economist print edition

Can Stephen Harper unite the right?

Get article background

AP

Harper and the remains of Day

SUCH is the political dominance of prime minister Jean Chrétien and his federal Liberal party, that some Canadians mutter, only half-jokingly that their country is becoming a one-party state. So Stephen Harper, chosen on March 20th as the new leader of the Canadian Alliance, the battered official opposition, faces an uphill task. Three days later, in Ontario, the Progressive Conservatives are due to choose a new leader who will automatically become premier of Canada's most populous province. Between them, the two new leaders will hold many of the keys to the future of the country's fractured right.

Mr Harper's election offers a fresh start to the Alliance, which has struggled since its foundation two years ago. He won by an unexpectedly wide margin, with 55% of the vote against 37% for Stockwell Day, the Alliance's outgoing leader. This decisive result should put an end to a debilitating leadership squabble.

Mr Harper, like Mr Day, is from Alberta (in fact, all four candidates were from Canada's most Americanised province, a sign perhaps of the Alliance's failure to spread its cause). He is best known for co-authoring an essay arguing that the province should erect a “firewall” between itself and the federal government, by measures such as setting up its own police force and pension plan. Still only 43, he is an articulate campaigner, a fiscal conservative free of Mr Day's born-again Christianity.

The Alliance represents an effort to broaden the political base of the western Reform party by wooing eastern Progressive Conservatives. Under Mr Day, it struggled. When Mr Chrétien called a snap election in October 2000, Mr Day increased the party's votes, but won only two seats in Ontario, home to one Canadian in three. He stumbled against Mr Chrétien in the House of Commons, and then faced a revolt by 12 of his 66 MPs.

Mr Harper inherits a party whose membership has fallen by more than half since the last election. Its long-term future depends on unity with the Progressive Conservatives. Mr Harper has ruled that out while Joe Clark, a former prime minister, remains the Conservative leader.

Another powerful figure on the right, Mike Harris, Ontario's premier since 1995, is bowing out this month. Mr Harris achieved national prominence with his “common sense revolution”, a Canadian version of Thatcherism. Only three of the five candidates to succeed him stand a chance. The one most likely to appeal to floating voters is Elizabeth Witmer, who pushed through labour and health reforms under Mr Harris, but now promises a more compassionate government. Unlike Ms Witmer, Jim Flaherty, the finance minister, would continue Mr Harris's tax cuts; he wants to cut spending further, abolish several ministries, and eliminate fraudulent claims for health care.

But the front-runner is Ernie Eves, Mr Flaherty's predecessor as finance minister, who implemented the tax and spending cuts before becoming a banker last year. As the best-known contender, for his campaign he has adopted the motto of a Olympic luge contestant: “lie flat, go fast and try not to die”. He has said that he would review a controversial system of school funding that gives funds to parents.

Whoever wins faces a tough provincial election in 2004. Mr Eves, the best placed of the three hopefuls,

trails Dalton McGuinty, the Ontario Liberal leader, by 14 percentage points. Mr Harris, a former golf professional, may have chosen the right moment to retire to the clubhouse.

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Japan

Reform in tangles

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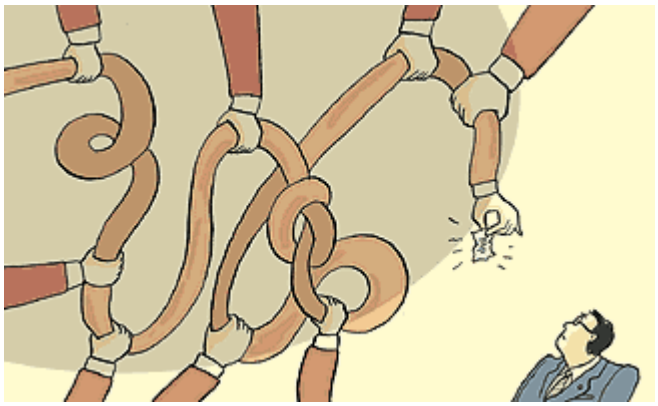

Until Japan's political system changes, attempts to tackle its economic woes will remain tied in knots

Get article background

YASUHISA SHIOZAKI starts tapping his finger on the dismal economic chart on his coffee table. “Unless we change the decision-making process,” he says bluntly, “we are not going to be able to solve this kind of problem.” With the economy in such a mess, it may seem a bit of a diversion to be trying to sort out Japan's political structures as well as its economic problems. But Mr Shiozaki, a 51-year-old MP from Japan's ruling Liberal Democratic Party (LDP), can hardly be accused of time-wasting. He has consistently prodded the government to take a firm hand to ailing banks, and has given warning against complacency after a recent rise in share prices. Far from being a distraction, his latest cause highlights how far Japan is from genuine economic reform.

Since co-writing a report on political reform, which was released by an LDP panel last week, Mr Shiozaki has further upset the party's old guard. Its legionaries, flanked by columns of the bureaucracy, continue to hamper most attempts to overhaul the economy. Junichiro Koizumi was supposed to change all that, by going over their heads and appealing directly to the public. Yet nearly a year after becoming prime minister, Mr Koizumi has precious little to show for his efforts. His popularity is now flagging and his determination is increasingly in doubt.

As hopes of immediate economic reform fade, optimists are focusing on another potential benefit of Mr Koizumi's tenure. They hope that his highly personalised style of leadership will pave the way for a permanent change in Japanese politics: towards more united and authoritative cabinets that are held directly accountable for their policies. As that happens, the thinking goes, real economic reforms will be able to follow.

Unfortunately, damage-limitation in the face of scandal too often substitutes for real reform. On March 15th, Muneo Suzuki, who had come under fire after a run-in with Makiko Tanaka—a popular foreign minister who was sacked in January—was himself drummed out of the LDP. He left just ahead of Koichi Kato, a one-time hero of the reformists who had been tarnished by the practices of his chief fund-raiser. Occasionally, these purges lead to useful changes. Ms Tanaka's successor at the foreign ministry, Yoriko Kawaguchi, is pushing new measures to keep track of contacts between MPs and her bureaucrats. More often, however, the scandals serve merely as distractions. What is really needed is an overhaul of the rules themselves.

A leading candidate for change is the 40-year-old system—informal but religiously followed—through

which the LDP machinery vets every bill before it ever gets to parliament. Most legislation starts in the LDP's party committees, which mirror the parliamentary committee structure. Proposals then go through two higher LDP bodies, which hammer out political deals to smooth their passage. Only then does the prime minister's cabinet get fully involved in approving the policy. Most issues have been decided by the LDP mandarins long before they reach this point, let alone the floor of parliament, leaving even the prime minister limited influence, and allowing precious little room for public debate and even less for accountability.

Consider Taro Kono, a second-term MP who collided with the system two years ago. While sitting on parliament's commerce committee, he had doubts about a bill on the reprocessing of nuclear fuel. He tried to raise these at the party's private committee meeting, with little luck. Then, when the party's leaders asked whether he would raise questions in the parliamentary committee—a public forum—Mr Kono admitted that he might not be able to restrain himself. So they booted him off the committee before he could get the chance. As a result, Mr Kono's opposition to the measure, which he had tried to voice from the beginning, was registered publicly only in a statement on his website.

To his credit, Mr Koizumi has made attempts to bypass this machinery. He began by choosing his own ministers, rather than accepting a team drawn up for him by the LDP party bosses. He has also relied heavily on a special economic advisory council, an outfit that first began meeting under his predecessor, Yoshiro Mori. These changes have made it a little easier for Mr Koizumi to formulate his own policies, independently of the party.

So far, though, he has fully exploited these resources only once. Mr Koizumi hopes to avert a health-care financing crunch by raising the portion of medical costs paid by some patients. When the LDP demurred, Mr Koizumi threatened to break with 40 years of precedent and send the bill directly to parliament. To avoid this calamity, the LDP's secretary-general cut a deal and had the party's top policy-making body rubber-stamp it. “I think the party blinked,” says Mr Kono. Even though Mr Yamasaki managed to preserve the façade of party approval, Mr Koizumi still succeeded in taking a radical shortcut, skipping two tiers of LDP machinery.

It was an important victory, for which Mr Koizumi has probably received too little credit. Yet Mr Shiozaki argues that Japan must go much further. For a start, taking on the LDP system through bluff and bravado is no substitute for clear institutional changes. Moreover, now that Mr Koizumi's popularity has plunged, he will find it harder to flout the party's rules. His proposals for tax reform, for instance, risk becoming bogged down, with his own economic council locked in dispute with both the LDP's tax committee and another committee dominated by bureaucrats.

As a result, progress will probably remain slow. Since they know that political reform leads to economic reform, and hence poses a threat to their interests, most of the LDP will resist any real changes. But at least a handful of insiders have now bought into one of Mr Koizumi's best slogans: “Change the LDP, change Japan”.

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Japan and South Korea

Political football

Mar 21st 2002 | SEOUL
From The Economist print edition

The World Cup is driving Japan and South Korea together—for now

Get article background

JAPAN'S prime minister could not have picked a more propitious time to travel to South Korea. After months of high tension last year, the two countries at last seem to be rubbing along a bit better. They have little choice if they want the 2002 World Cup soccer competition, which they host together this summer, to be a success. Junichiro Koizumi's three-day visit to Korea, which started on March 21st, and his meetings with Kim Dae Jung, South Korea's president, seem intended to build on a new sense of partnership. But will the current friendliness last? There are two obstacles: Japan's continued reluctance to make full amends for its wartime atrocities, and its hawkish stance towards North Korea.

Relations between South Korea and Japan have always been volatile. They began to improve four years ago, during Mr Kim's visit to Tokyo, when Keizo Obuchi, then Japan's prime minister, offered his “heartfelt apology” for Japan's colonisation of Korea, which lasted for 35 years until 1945. With improving relations came a sharp increase in tourism and trade between the two countries.

But the upswing did not last long. Last April, a group of Japanese right-wing scholars published a history textbook which failed to mention that thousands of women from Asia, mostly from Korea, were made to work in Japanese army brothels. It also put a positive gloss on Japan's occupation. Mr Koizumi aggravated the sore with an official visit last summer to the Yasukuni shrine, where Japan's war dead, including war criminals, are venerated.

Mr Koizumi has tried hard to patch things up since then. He made a seven-hour visit to Seoul last October to tour a prison in which many Korean resistance fighters were tortured during Japan's colonial rule. While there he again apologised for Japan's aggression. He also agreed to commission a group of Japanese scholars to co-operate with the South Koreans to pin down any distortions in Japan's history books. On top of this, Japan eased immigration rules earlier this year to allow South Korean passport holders a longer stay in Japan—up to 90 days, the same as Americans and Europeans get, rather than two weeks. But these efforts to restore relations with South Korea will go out of the window if Mr Koizumi (or a successor) pays another visit to Yasukuni.

The other contentious issue is North Korea. Mr Koizumi seems to side with George Bush, who included North Korea as a member of the “axis of evil” along with Iraq and Iran. Japan wants to see a number of its citizens, abducted by North Korean agents years ago, return home and fears the North's missiles. His stance is unpopular with Mr Kim, who has pursued a “sunshine policy” of trying to thaw relations with the communist regime by supplying aid.

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Afghanistan

Unhappy new year

Mar 21st 2002
From The Economist print edition

Afghanistan's difficult reconstruction

Get article background

THE Afghan new year, which started on March 21st, brought little cause for celebration. Even as it declared victory in Operation Anaconda—a bitterly-fought, two-week American-led battle to crush a large pocket of Taliban and al-Qaeda forces in eastern Afghanistan—the United States was stressing that much more fighting lay ahead. “There are still thousands of trained al-Qaeda killers on the loose,” said George Bush on March 19th. Almost as he spoke, allied troops in Khost were under fire from mortars and machineguns. Against that sombre background, Britain said it was sending a 1,700-strong force of marines and army artillery to join the battle. This will be Britain's biggest combat deployment since the Gulf war of 1991.

The remaining Taliban and al-Qaeda fighters, however, are only part of the problem. Local Afghan officials have already given warning that the coalition victory in Paktia province could prove to be Pyrrhic if it exacerbates local feuds. A contingent of Tajik forces sent to join the fighting by Hamid Karzai's interim administration in Kabul has notched up military successes but risks alienating the local population, which is mainly Pushtun. In addition to such ethnic tensions, competing warlords and plain banditry also add to the general insecurity outside the capital. And yet the interim government's foreign supporters have so far, despite intensive discussion, been reluctant to expand the 4,500-strong International Security Assistance Force, or to extend its mandate beyond Kabul.

The security situation is not preventing at least some Afghan refugees from going back home. Since March 1st, more than 60,000 people—twice as many as were expected—have returned from Pakistan with the help of the UN High Commission for Refugees (UNHCR). The agency expects that about 800,000 refugees will return to Afghanistan this year, and an additional 400,000 who fled their homes but stayed inside the country should make their way home too. Even so, many are still travelling in the other direction. About 60,000 Afghans lined up at the Chaman border crossing with Pakistan during January and February. Many are fleeing poverty, but others are Pushtuns, the tribe that made up the backbone of the Taliban regime and are now being persecuted.

Until Afganistan becomes richer and safer, the flight will continue. And yet only a small fraction of the money promised last January at the Tokyo aid conference has trickled in. Since the UN appealed for funds in October, a mere $671m has been received, most for emergency food and refugee assistance. The UN estimates that half of the $1.1 billion still needed for this year will have to be spent on humanitarian assistance. Food is still scarce, and most of the 3.5m Afghan refugees still need to be cared for.

But foreign money is also needed to keep the machinery of central government running. Since its creation in December, the interim administration has been surviving on international handouts channelled through a UN Development Programme (UNDP) trust fund. Cars and office equipment for ministries have been sent from abroad. Plumbers, masons and electricians have been called in to patch up derelict government buildings. The first cash contribution for the new government was flown in in a suitcase to be deposited in the empty central bank.

Thanks to the UNDP fund, about 60,000 civil servants, mostly based in Kabul, are now receiving salaries,

even if they are only $28 a month. The system is slowly being expanded to the provinces. When schools open on March 23rd, some 50,000 teachers should be on the payroll. The trust fund, however, has received about half of the $50m it needs to operate until the end of July, when it is expected to fold. Until the government is able to collect taxes, civil servants' salaries and day-to-day expenses will have to be paid out of international purses. The interim administration is putting the final touches to the government budget for the year starting on March 21st. Out of a total of $400m or so, $350m will have to come from outside.

As with humanitarian help and government salaries, the long-term reconstruction of Afghanistan will depend on foreign aid. Property agencies and souvenir shops are booming in Kabul; but there are few telephones, no factories to speak of, and few good roads. The few surviving banks have not taken deposits, let alone made loans, in years. Money for reconstruction will not begin to flow for a few months yet. Donors have to negotiate an obstacle course of bureaucracy before cash can be released. And even when the cheques are ready for signature, it will take an age to spend the money effectively—and keep track of it.

The continuing flow of aid also depends on this fractious country's ability to comply with the political road map that was charted for it in Bonn. A *loya jirga*, or council of tribal leaders, is supposed to convene before the end of June to nominate a government that will rule for 18 months. An independent commission is still trying to work out who should sit on the council. One point in its favour is that it is to be chaired by Mohammed Zahir Shah, the country's 87-year-old former king. The former monarch has said that he has no desire to resume his reign. But many Afghans, nostalgic for the happier days associated with his reign, are eagerly awaiting his return from exile before the end of this month.

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Property rights in China

Landlords of the world, unite!

Mar 21st 2002 | BEIJING
From The Economist print edition

The well-off stand up for their rights

IT HAD all the trappings of real political protest: huge signs with hand-painted Chinese characters screaming out about injustice and blood debts, angry crowds marching in the streets of the capital, and sporadic outbreaks of violence as hundreds of frustrated protesters charged a hefty brick wall and battered it to pieces. China's disenfranchised masses rising up against the system? Not quite. Instead, they were the rich and nearly rich, acting to protect their wealth.

The protesters, late last year, were the owners of smart new properties in the Atlantic Place apartment complex in north-eastern Beijing, who objected when they discovered that the parkland, lake, tennis courts, swimming pools and clubhouse they had been promised were being scaled back in favour of more flats. The lost amenities and added population density, they said, would cut their property value by a third, and they were not going to take it lying down. Similar disputes have arisen in at least half a dozen other luxury Beijing housing estates in recent months.

The flats at Atlantic Place range in price from 500,000 yuan to 1m yuan ($60,000 to $120,000). Some of the owners are professionals who could only manage the step-up in lifestyle with the help of bank loans; a handful are wealthy speculators owning ten or more flats and leasing them out. But they all smelled something fishy about the way the developer and the city planning officials engineered changes in the plan after they had bought their flats. Establishing an owners' committee, they acted together to organise protests, and hire a lawyer to help them navigate the murky intersection between China's rickety legal system and its corruption-prone administrative structure.

Last month they launched a suit in a municipal district court, charging not the developer, but the city planning bureau with illegally revising a previously approved plan. Shortly afterwards, the developer settled out of court, agreeing to restore most of the original plan. Tony Huang, a manager at Atlantic Place, insisted there was never any intention to cheat the owners but acknowledged the settlement, and attributed the dispute to a lack of clarity in Chinese property laws.

Wang Yanbin, a high-tech entrepreneur who owns a flat at Atlantic Place, reckons such protests are a healthy sign of the social and economic progress China has made. “Twenty or 30 years ago, no one had property and so no one had interests to defend,” he says. Not that there isn't still a long way to go: the Beijing municipal propaganda bureau has acknowledged that local media were ordered to suppress reporting of the protests because senior officials worried about their potential impact.

Dali L. Yang, a political scientist at the University of Chicago, says that such protests have become a significant driver of social change in China, despite the government's obvious concerns about where the trend could potentially lead. “As long as the protesters focus their attention narrowly on the issues that concern them, the government has been willing to listen,” he says. He predicts that relevant rules and enforcement will be tightened to keep developers honest, and that “such day-to-day demands by ordinary folk will continue to make China a better place.”

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Indonesia

Accountability on trial

Mar 21st 2002 | JAKARTA
From The Economist print edition

There is less to Indonesia's spate of court cases than meets the eye

EPA

Suharto junior, in the dock

AS TOMMY SUHARTO, son of the former dictator, went on trial for murder this week, his lawyers suggested he had been subjected to character assassination by the Indonesian media. If so, it would mark a tremendous reversal of fortune: in his days as a privileged playboy, Tommy had little to fear from the press. If they could not be bought off, they would be intimidated or in extreme cases closed down by the man no one dared to oppose.

Today Suharto senior is lying at death's door in his house in Jakarta's Cendana Street. But there are fears that his ideas about how to govern the country are being revived by his former opponent, President Megawati Sukarnoputri. Many believe Tommy's trial for the murder of a Supreme Court judge, Syafiuddin Kartasasmita, is nothing but a showpiece, and that a lenient sentence has already been fixed in advance.

If that happens, it will not be the first attempt to bring some accountability into Indonesian politics to misfire. With the backing of Miss Megawati's party, the country's legislature this week voted not to investigate allegations against its speaker, Akbar Tandjung, chairman of the older Suharto's former ruling Golkar party, who is under arrest on corruption charges.

Mr Tandjung may have been arrested by the attorney-general's office, but he has not been removed from his post, nor has he resigned. And there appears to be little chance he will. The central bank's governor, Syahril Sabirin, has just been sentenced to three years over the 1999 Bank Bali scandal, but is still refusing to resign, hiding behind a law that makes it virtually impossible to fire the central-bank chief. And Mr Syahril is the only key actor in the Bank Bali affair who has even been sentenced. The others, mostly senior figures in Golkar, either never made it on to the list of defendants or were let off by the courts.

Like Mr Suharto before her, Miss Megawati and her supporters are said to find criticism hard to take. She frequently lambasts the media. She never gives press conferences or interviews. She has also reinstated the notorious information ministry, which under Mr Suharto licensed publications and frequently closed down ones it did not like. A state-secrets bill is likely to be passed in the next few months, a device which is used in Singapore and China to intimidate journalists into not writing critical stories. And last week, the government withdrew the accreditation of a foreign correspondent for the first time since the Suharto regime fell.

Lindsay Murdoch, correspondent of the *Age* and the *Sydney Morning Herald*, had been in Indonesia for three years, winning several awards for his coverage. But when he wrote a story about how Indonesian soldiers in the troubled province of Aceh had poured boiling water over a four-month-old baby, who subsequently died, it clearly touched nerves.

The weakness of Miss Megawati's government, an awkward coalition of Islamic and non-Islamic groups, does not help. Her trump card is that she is close to the armed forces, Mr Suharto's former power base. To protect it, she appointed several retired generals to her cabinet.

On March 14th, Indonesia finally convened the first of its special human-rights courts on the 1999 East Timor violence. On trial were a former governor, Abilio Soares, and former police chief, Timbul Silaen. The trials rapidly got bogged down in legal challenges. Notably absent were any generals. There are no

plans to try the people who oversaw the violence, in particular the former military chief, General Wiranto. Accountability in Indonesia, it seems, still has a long way to go.

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Pakistan

Christians as targets

Mar 21st 2002 | PESHAWAR
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The new symbols of anti-Americanism

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KILLINGS carried out as a result of religious differences are frequent in Pakistan. But mostly they are the result of tensions between Shia and Sunni Muslims. Christians, no more than 1% in a population of 120m, have until recently largely been left in peace. The attack on a church in Islamabad, the capital, on March 17th, in which five people died, two of them Americans, was linked more to the war in Afghanistan, rather than directed specifically against the Christian faith. An attack on a church in Bahawalpur, in Punjab province, in October, in which 18 people died, was the worst suffered by Christians since Pakistan was founded, and was also linked to the Afghan campaign.

After September 11th, and Pakistan's support for the American-led war against terrorism, local Christians feared that they might become symbolic targets. President Pervez Musharraf promised them security. The Islamabad church is in the diplomatic quarter of the capital and supposedly closely guarded, but terrorists hurling grenades got through anyway. The Bahawalpur church was guarded by two Muslim policemen. Both were shot dead.

Some Christian clergy are telling their congregations to follow the principle of turning the other cheek. It is a sentiment that would have found favour with Muhammad Ali Jinnah, the founder of Pakistan in 1947. Although Pakistan is a Muslim state rather than a secular one, he assured the minority of Christians converted by missionaries when Britain ruled the subcontinent that he regarded religion as a personal matter.

Religious co-existence prevailed for some 30 years until the 1980s when Pakistan's then military ruler, Zia ul Haq, introduced blasphemy laws to gain the support of religious parties for martial law. Merely stepping on a newspaper that contained a verse from the Koran could be construed as a blasphemy. Any blasphemy could be punishable by death. Unscrupulous Muslim landlords accused Christians of blasphemy in moves to grab church lands, many of which were productive and valuable. Greed was their motivation rather than a clash of faiths. However, the cry of “blasphemy” can rouse passions among the mob, whether true or not, and in 1997 rioters ransacked 13 churches and a school in southern Punjab.

In 1998 a Christian family of nine was killed in the northern city of Nowshera. This led to a rally in Lahore protesting, among other matters, that Christians were being discriminated against. They object to being given a quota of seats in parliament and in local assemblies, and seek an end to separate electorates. Last year many Christians boycotted local elections. All non-Muslims are part of a quota system.

Mr Musharraf is no doubt too busy to concern himself with the minutiae of election law. But he is desperate to find the perpetrators of the recent attacks, and to protect other Christians. He phoned George Bush to express regret for the deaths of the Americans, the wife and daughter of a diplomat, and to tell him that senior police officers in charge of security in Islamabad had been moved. Mr Bush said he would send his own agents to Islamabad to help hunt the killers. Turning the other cheek may not be his priority.

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Unrest in Central Asia

The shock of dissent

Mar 21st 2002 | ALMATY
From The Economist print edition

Warnings for two governments

IT IS unclear what started the brutal clashes: stone-throwing by demonstrators or the police opening fire. What is certain is that five people are dead and dozens have been injured as a result of two days of violence this week, the worst in Kirgizstan's ten years of independence. For the first time too, the authorities in this small Central Asian country kept order by firing into a crowd.

The demonstrations, involving more than 2,000 people in the southern province of Jalal-Abad, were over the trial of a member of parliament, Azimbek Beknazarov. A shaken government suspended the trial and released Mr Beknazarov, who had been charged with abusing his office seven years ago as a regional investigator.

The affair has undermined the authority of President Askar Akaev's government. The case is seen to have been botched by officials. Properly handled, it is believed, the disorder could have been avoided. In the Jalal-Abad region, one of the poorest in this country of 5m people, tribal and blood relations are strong. Why was one of their own, whom they had elected into office, kept in jail for more than two months before being brought to trial? Some are suspicious that Mr Beknazarov is really being persecuted for daring to criticise the government for ceding too much territory to China in a border agreement. Others say the underlying reason for the riots was people's exasperation with corruption, and the government's failure to provide key services.

Mr Beknazarov, now a national figure, was relatively unknown before his arrest. The incident has received more international attention than it would have a few months ago. Kirgizstan has become important in the American-led war in Afghanistan. Around 1,500 coalition soldiers are stationed at an airbase outside the Kirgiz capital, Bishkek.

The government may be repeating the error made by other Central Asian leaders: of trying to stifle reasonable dissent, and thereby creating real enmity. However, a high-ranking foreign diplomat says that he believes there are people in the government well aware that the stability of the country depends on talking seriously to those with opposing views.

Dissent may be growing in Central Asia, even in Turkmenistan, one of the most tightly controlled places on the planet. Several top diplomats have defected recently, including Boris Shikhmuradov, a former foreign minister. He now styles himself leader of the Turkmen opposition. Its target is the country's president, the self-styled Turkmenbashi (Father of Turkmen), who has constructed a personality cult rivalled only in North Korea, and is squandering his country's mineral wealth on sprawling palaces and golden statues of himself. Seemingly rattled, the Turkmenbashi has this week been purging his extensive security apparatus—live on television.

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Vietnam and China

Trading places

Mar 21st 2002 | MONG CAI
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Competition breeds contempt

THE northern Vietnamese town of Mong Cai is one big bazaar. But shoppers would be hard-pressed to find any local goods. The mammoth bales of knock-off clothes, complete with their “Made in Italy” labels, are smuggled across the nearby border from China. So are the endless piles of cooking pots, suitcases, car parts, stationery, toys, mobile phones, plastic plants and erotic figurines. The food comes from China, too, a vendor in the fruit and vegetable market explains. The only local goods she can come up with are some eggs—but, she hastily adds, she also has some cheaper Chinese ones. Even the stall owners are Chinese, and the market starts winding down at 3pm, because the border closes at 4pm.

This petty trade with China has flourished since the border between the two countries first opened in 1990, as smugglers learned to evade border patrols and pay off local policemen. In more recent years, official trade has also blossomed, from $955m in 1998 to $3 billion in 2001. Indeed, Vietnam's trade with China is growing faster than that with any other country—despite the conclusion of a trade agreement with America in 2000.

The signs of the growing economic ties are everywhere. The road to Mong Cai is being widened, as is that to another border post in the northwest. The road to the main crossing point was upgraded last year. Chinese tourists are flooding south along these new arteries. In 2000, over 600,000 of them visited Vietnam, by far the largest number from any country. In Mong Cai, a hotel and casino caters exclusively to gamblers from across the border (Vietnamese are barred from such decadent pastimes). Minibuses whisk them straight from customs to the 24-hour facility, where the minimum stake is $10.

Yet not all Vietnamese are delighted about these ties. Suspicions endure from the brief war the two countries fought 23 years ago. Although they recently managed to agree on where their land border lies, they are still arguing about the division of the sea. The pair have Confucianism and communism in common, yet that seems only to increase Vietnam's desire to escape from China's shadow. Vietnamese like to moan about the shoddiness of Chinese goods, and deplore their neighbours' supposedly uncivilised habits.

But that sort of prejudice seems to be galvanising Vietnamese officials. The government must reduce business costs, they say, so that Vietnamese goods can compete with Chinese ones. They talk about trying to join the WTO, so that they can vie with China for investment. The tradesmen of Mong Cai, it seems, are helping to set Vietnam's economic policy.

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Zimbabwe and Africa

The friendlessness of Robert Mugabe

Mar 21st 2002 | JOHANNESBURG
From The Economist print edition

Zimbabwe's suspension from the Commonwealth is good news for Africa

Get article background

IT WAS only a symbolic punishment, but symbols matter. On March 19th, the leaders of South Africa, Nigeria and Australia agreed, unexpectedly, to suspend Zimbabwe from the Commonwealth, a club composed largely of Britain's ex-colonies. Suspension carries few direct, practical consequences. It does not trigger economic sanctions, and it could even discourage some, such as the European Union, from tightening the mild sanctions currently in place. President Robert Mugabe's government quickly dismissed the decision as unimportant.

But the decision will, nonetheless, sting Mr Mugabe and may weaken his grip on power. It followed a report by Commonwealth observers that last week's presidential election, which Mr Mugabe “won”, was conducted in a “climate of fear”. And, crucially, it represents the first serious, public criticism of Mr Mugabe by the leaders of Africa's two most influential countries, Thabo Mbeki of South Africa and Olusegun Obasanjo of Nigeria.

Until now, Mr Mugabe could plausibly claim that his fellow Africans supported him. Five African presidents turned up at his inauguration on March 17th, and South Africa's deputy president, Jacob Zuma, gave him a big hug and called his win “legitimate”. When Mr Mbeki and Mr Obasanjo visited Harare, Zimbabwe's capital, this week, they called for reconciliation between Mr Mugabe's government and the opposition. South Africa has long touted the idea of a government of national unity for Zimbabwe, and many observers believed that Mr Mbeki would oppose suspension in favour of more talks.

Mr Mugabe will henceforth find it harder to portray his opponents as merely arrogant whites and their black lackeys. Decisions by Switzerland and New Zealand to impose targeted sanctions on members of Mr Mugabe's inner circle, and Denmark's ending of aid and the closure of its embassy in Harare, could easily be dismissed as acts of spite by white supremacists. But now his is the first elected government to be excluded from the Commonwealth for contravening the democratic principles agreed, as it happens, at a conference in Harare in 1991. This leaves Mr Mugabe isolated. The Movement for Democratic Change (MDC), Zimbabwe's cheated opposition party, said it was “delighted and surprised” by the suspension and called for fresh, internationally-supervised elections. On March 19th, trade unionists launched a three-day strike to protest against intimidation by the police. But the police banned it, and it fizzled.

Mr Mugabe may believe he can brazen out further protests and international criticism, even from fellow

Africans. He has reportedly refused, in conversation with Mr Mbeki and Mr Obasanjo, to consider sharing power with his rival, Morgan Tsvangirai. Since the election, he has pressed ahead with a bill aimed at stifling independent journalism in Zimbabwe, promised to accelerate his programme of seizing white-owned farms, and hinted that white-owned businesses may be next. On March 20th, Mr Tsvangirai was hauled into court and charged with treason, for allegedly having plotted to kill Mr Mugabe.

Despite his bravado, Mr Mugabe may still buckle. Thanks to his misrule, Zimbabwe depends on South Africa's generosity for its electricity and on food aid to prevent many of its people from starving. Foreign pressure may force him to talk to the opposition. Mr Tsvangirai says that “meaningful, substantive talks” are inevitable, but will take place only when Mr Mugabe calls off his thugs. The MDC says that several of its polling agents and supporters have been abducted, beaten and even killed since polling finished.

Beyond Zimbabwe

Whether or not Zimbabwe's suspension spurs Mr Mugabe to behave, it will restore some credibility to the Commonwealth, which had seemed indecisive and racially divided. It will restore confidence in Mr Mbeki; the South African currency, the rand, rallied on the news. And it may save Mr Mbeki's grand plan for an African revival. Along with Mr Obasanjo and others, Mr Mbeki has proposed a “New Partnership for African Development”, which he hopes to pitch to the G8 industrialised countries at a meeting later this year in Canada. In exchange for more aid and freer trade, African countries are supposed to demonstrate their respect for good government and the rule of law.

The plan calls on African governments to “peer review” their neighbours. Though it galls Mr Mbeki, Zimbabwe was widely seen by outsiders as the first test of this procedure. Mr Mbeki insists that it is too early to judge his project, but Britain and America said that a cloud would hang over the proposal if Mr Mbeki stood by while Mr Mugabe stole an election. When Mr Mbeki failed to condemn Mr Mugabe's pre-election campaign of terror, the South African's warm relationship with Tony Blair, Britain's prime minister, grew frosty.

That should now change. Mr Mbeki may not be entirely happy about Zimbabwe's suspension. Both he and Mr Obasanjo were tight-lipped during the announcement, leaving John Howard, the Australian premier, to answer questions. On March 20th, the South African government formally recognised Mr Mugabe's victory, despite what it called “weaknesses” in the electoral process. But still, Mr Mbeki can now argue that “peer review” means something, and that some African leaders take democracy seriously.

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Saudi Arabia's crown prince

A man with a plan

Mar 21st 2002 | CAIRO
From The Economist print edition

A chain-smoking champion for the Arab world

Get article background

AP

A modern sort of royal

IN THE absence of regular free elections, it is tricky to gauge the popularity of Arab leaders. But one gruff, bluff old man is attracting the kind of praise not heard in the souks since Egypt's Gamal Abdul Nasser preached pan-Arabism and cocked a snook at Britain in the 1950s and 1960s. His name is Crown Prince Abdullah of Saudi Arabia. His lustre owes much to the shortcomings of his peers—most of the region's potentates and presidents-for-life are too busy clinging to power to project any wider vision. But his plan to bring peace to the Middle East is being taken seriously, and will be the main topic of debate at an Arab summit in Beirut next week.

The tenth of 36 brothers, Abdullah was dismissed by one Saudologist as “gentle but incompetent” when he became heir to the Saudi throne in 1982. Yet, since his older brother, King Fahd, suffered a stroke in 1995, the 78-year-old prince has shown a talent for leadership. At home, he has impressed liberals by opening up to foreign investors, tolerating mild criticism of the government and hinting that more women should be allowed to work. Conservatives, meanwhile, like his forthright manner and rare reputation for personal probity. By bluntly admitting Arab failings, yet committing himself to Arab causes, he has won respect abroad. Saudi Arabia is being listened to, not just because of its oil wealth but because, for a change, it has something to say.

At recent Arab summits, the physically imposing, chain-smoking prince has been a dominant presence. Next week in Beirut, delegates will ponder his proposal that Arab countries should pledge “complete peace” with Israel in return for a full withdrawal from lands occupied in 1967. The proposal has attracted its share of critics. It is nothing new, say some, since other Arab leaders have made similar offers before. It is a non-starter, say others, since Israel will never surrender all the land, and since it ignores tricky issues such as Jerusalem and the fate of Palestinian refugees. The initiative's backers counter that Israelis and Palestinians have their fingers so locked around each others' throats that they need reminding of what a real regional peace, and not just a pause in the smiting, could look like. They also note that Abdullah has hinted that the details are negotiable.

But the best thing about the plan is its author. Under Abdullah, Saudi Arabia has emerged as the Palestinians' most determined and credible champion. Speaking to the Saudi army before the 1991 Gulf war, the prince expressed regret that his men were being sent to fight Iraq, rather than joining Iraqis to “reclaim our usurped rights in Palestine”. Last year, angered by what he saw as an American tilt towards Israel, he turned down an invitation to President George Bush's ranch in Texas, and later sent a letter threatening to end the 60-year-old Saudi-American alliance.

Since the outbreak of the current *intifada*, the kingdom has bankrolled Yasser Arafat to the tune of some $400m. Without such funding, what is left of the Palestinian Authority, including its security forces, would collapse. This gives the Saudis obvious leverage with the Palestinians, but they are also well placed to prod the shaky and recalcitrant governments of Syria and Lebanon into negotiations.

In appreciation of Abdullah's growing influence, President Bush has again invited him to his ranch. Abdullah accepted, partly out of gratitude for Mr Bush's efforts at peacemaking, but also because he wants to mend relations that have been tense since it emerged that most of the terrorists who attacked America on September 11th were Saudis. To this end, he has also opened the secretive kingdom to

unprecedented press scrutiny, at one point greeting reporters in his garden wearing running shoes. Abdullah is not about to turn Saudi Arabia into a playground for the Pentagon or a liberal democracy. He is not likely to shake the country's rigidly conservative mores. But he does have one quality that America might find useful: credibility with his own people.

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A murder trial in Congo

Who killed Laurent Kabila?

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From The Economist print edition

Some 50m people had a motive

A MURAL depicting a lavish picnic—roast chickens, bottles of wine and massive bowls of fruit—adorned the wall behind the judge's bench. Somewhat incongruous for a courtroom, but the most eagerly anticipated murder trial in recent Congolese history is taking place in an old, partially-converted eating hall in Makala prison in Kinshasa, the capital. A hundred and fifteen people are accused of plotting the (successful) assassination of Laurent Kabila, the Democratic Republic of Congo's president, in January last year.

When the trial opened on March 15th, there were not enough chairs, so half the defendants had to stand. They are used to suffering. Most were arrested a year ago, and have remained in cells ever since. Congolese jails are not comfortable, and many of the defendants are said to have been tortured. None has been formally charged; the opening day of the trial was the first time any had met their lawyers.

Little has been revealed about Mr Kabila's death. The official story is that the corpulent despot was shot through the neck by a bodyguard, who was in turn killed shortly afterwards. An investigation found evidence of an “international plot”, involving rebels allied with Rwanda, numerous unnamed foreign intelligence agencies and a mystery poisoner. It is not clear how the 115 defendants fit into this theory. Most are soldiers; the best-known is Colonel Eddy Kapend, Mr Kabila's cousin, who was responsible for his personal security. The 40 civilian defendants include Fono Onokoko, the 19-year-old wife of the man said to have pulled the trigger. Mr Kapend is alleged to have dreamt up the plot, silenced the assassin and mobilised troops in preparation for a coup. It is not clear what Ms Onokoko is supposed to have done. Human-rights groups suspect that she and others were arrested simply for having the wrong relatives or friends.

Congo's new unelected president is Mr Kabila's son, Joseph, who has said little about the whole affair. He inherited a country split and charred by war, but unlike his father, he has tried to improve matters, by calling a ceasefire, welcoming UN military observers and talking to the rebels. But the latest round of peace talks, in the South African casino resort of Sun City, has seen little progress. Mr Kabila's negotiators stomped out on March 14th, after rebels and their Rwandan backers attacked a town in eastern Congo. The negotiators' exit has prompted an outcry back home in Congo. Was the trial in Kinshasa intended to divert attention from Sun City? Or vice versa?

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War crimes in Sierra Leone

Caged, but unlikely to hang

Mar 21st 2002
From The Economist print edition

Foday Sankoh, the rebel whose troops severed countless limbs, is on trial

Get article background

VISIBLY thinner and weaker after two years in detention, Foday Sankoh is finally in the dock. He was sentenced to death in 1998, but then pardoned, as part of a peace agreement between his rebel army, the Revolutionary United Front (RUF), and the government of Sierra Leone. Mr Sankoh allegedly carried on having people chopped up, however, and is now answering to a local court. If it finds him guilty, it could put him to death.

After a decade of civil war that left an estimated 50,000 dead, things are looking brighter for Sierra Leone. The fighting appears to be over, the rebels and the pro-government militias have disarmed, and elections are scheduled for May. A state of emergency, under which the authorities could detain anyone they liked, was lifted on March 1st. Mr Sankoh was formally charged largely to keep him behind bars.

The timing of the trial is awkward, however. The government is trying to do things by the book, but Sierra Leone's courts are in a mess, so it will be hard. More worryingly, the humiliation of their leader could spur ex-rebels to destabilise the fragile country before voters have a chance to go to the polls. So far, Mr Sankoh's appearances in court have attracted little more than curiosity. But according to a spokesman for the RUF's political reincarnation, he remains the party's presidential candidate, even from his cell.

The rebel leader is also a prime candidate for a special war-crimes tribunal, which is to be set up by the UN and the Sierra Leonean government. If the delays that dogged similar courts dealing with Rwandan and ex-Yugoslav war criminals are any guide, trials will probably not kick off for at least another year. Although the special tribunal will have precedence over any local one, the situation could become complicated were Mr Sankoh sentenced to death in the local court before the tribunal—which will be able to hand out only prison sentences—has a chance to take on his case. But Rodolfo Mattarollo, in charge of the UN human-rights unit in Sierra Leone, says that this is unlikely to happen. Sifting through the 70 charges levelled against Mr Sankoh, and dozens of other cases besides, will take the local court a long time. If he is handed over to the tribunal before his current trial ends, Mr Sankoh will escape the noose.

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Kenya

No swots, please, we're Masai

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From The Economist print edition

Why the Masai send their slower children to school

AP

“WE PICK out the brightest children, those with the most potential, and then send them off with the goats,” explains Johnson Kinyago, a Masai herder. “It takes brains to identify each animal, find water, and ward off cattle rustlers. School is for those who are less quick.” Mr Kinyago has two sons. The brighter boy tends his flocks; the other has to go to school. By Masai standards, Mr Kinyago's is a studious family: only 35% of the children of Kenyan pastoralists attend classes. Herders rely on their children's labour, so many feel that time spent leafing through books is wasted. Barely one Masai in ten can read, which leaves the tribe less than ideally placed to take advantage of the information age.

Most Masai live much as they have for centuries. Masai warriors puncture and stretch their ear lobes to make all-flesh ear-rings, and Masai brides knock out some of their front teeth to add to their allure. Sadly, proud traditions fill no stomachs, and since their illiterate forebears signed away 90% of their land to the British, the Masai now have too little pasture to sustain a swollen population. In drought years, many of their cows die and they subsist on food aid.

To help their people cope, a group of educated young Masai are setting up informal classes under thorn bushes. In one district, 1,800 young herders have so far been taught basic literacy, Swahili, English and maths. Around 100 have graduated into the formal education system, and many of the rest have learned enough to decipher the English instructions on packets of veterinary drugs, and to haggle more competently with livestock traders.

Masai youths win respect by doing “warrior service” guarding cattle, but these days there are often more warriors than cows. One young warrior, Samia Sashore, carries a spear in one hand and his mother's shopping in the other. “There's not much for a warrior to do these days,” he says, “There are eight of us in my homestead and two cows.” After eight years as a warrior, he has now started school. His ambition is “to learn Swahili and get a job.”

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About sponsorship

France's presidential election

Two splendid programmes, spot the difference

Mar 21st 2002 | PARIS
From The Economist print edition

France's presidential campaigners unveil their glorious plans and promises

Get article background

PROMISES, promises. Should French voters take Jacques Chirac, their conservative president, and Lionel Jospin, their Socialist prime minister, at their word? If so, it will hardly matter which one wakes up on May 6th to preside for the next five years over a country which is simultaneously a nuclear power, a permanent member of the UN Security Council and the third-biggest economy in Europe. In either case, France will supposedly be richer, more competitive, more caring and—above all, given the voters' preoccupation with crime—safer. Indeed, Mr Chirac has borrowed the New York concept of “zero tolerance”. For his part, Mr Jospin has borrowed a Tony Blair line, pledging like Britain's prime minister to be “tough on crime, and tough on the causes of crime.”

But, as France's cynical electorate is well aware, it is easier to make the promise than to fulfil it. Mr Chirac's “commitment to France” comes in the form of 12m copies of a 24-page booklet listing eight separate promises, from pushing back the rising tide of crime (now running, according to the president's calculator, at one infraction every seven seconds) to “working to humanise and take control of globalisation”. On paper, Mr Jospin's commitment is even greater: a 40-page brochure, albeit in a mere 8m copies, that lists ten promises, from reducing the numbers of jobless to cancelling third-world debt. Look through both booklets and even the party faithful would be hard-pressed to find the substance to back the candidates' wish-lists.

Where, for example, is the arithmetic to back Mr Chirac's promise that over five years income tax can be reduced by a third, even as he puts more money into health care and education? His cuts in income tax and social charges alone add up to *euro*30 billion ($26 billion) over five years. Similarly, if France is to stay within the budgetary straitjacket set by the EU, how exactly will Mr Jospin (whose promised tax-cuts amount to *euro*18 billion) pay for a new child-care allowance, for vocational training for the young, for housing for all (by 2007 there are to be no homeless people on France's streets), for an Internet-linked computer for every five primary-school children, and so on? And meanwhile how can he airily promise to lower the number of jobless by 900,000 (“Why not a million?” sneered one Chirac-supporter)?

Such questions may be a bit unfair. As Mr Jospin pointed out at his manifesto's launch on March 18th, the calculations are based on an average economic growth rate of 3% a year—but the government's burden will be shared with the employers and the unions, and precise shares remain to be negotiated.

Moreover, the questions surely miss the point: what the voters want to know is what the candidate stands for, not just how he will pay for it.

In which case, they need to look not just at where the programmes overlap—as they do on crime (both envisage a "super-ministry" to co-ordinate France's rival police forces and gendarmerie), the protection of the environment, the "mastering" of globalisation and the need to lower taxes—but where they differ.

In essence that boils down to two thorny problems: managing a shorter working week and providing for a growing number of retirees dependent for their pensions on an increasingly hard-pressed proportion of tax-paying workers.

When Mr Chirac mistakenly dissolved parliament five years ago, it was the promise of a 35-hour week for the same pay as 39 hours that helped bring Mr Jospin's left-wing coalition unexpectedly to government. Not surprisingly, therefore, the prime minister glosses over the problems of its implementation. Instead, his programme repeats a worker-friendly theme: a special account to give each worker the right to life-long training; a "back-to-work" contract for 200,000 jobless people aged 50 or more; more workplace negotiation with unions that are more representative of their members; seats for employees on company supervisory boards; individual assistance for the young to seek training; and more subsidies to encourage firms to hire more workers.

By contrast, Mr Chirac, while happy to promise public-sector jobs and special help for the young, strikes a more boss-friendly note: with the aim of creating 460,000 jobs, social charges will be lowered to their level of 1993-95; corporation tax will be reduced; and help will be given to stimulate the creation over the next five years of 1m new firms. More to the bosses' taste, Mr Chirac calls for a "negotiated relaxation" of the 35-hour week: let the willing and able "work more to earn more."

As for pensions, Mr Chirac is nicely vague: the "pay-as-you-go" system, with today's workers paying for today's pensioners, will be guaranteed and corporate savings schemes encouraged—but there will also be "pension funds *à la française*". What that implies, in Mr Jospin's view, is a slippery slope towards the "Anglo-Saxon" model of private-sector pension funds. But how would a President Jospin, ideologically committed to the present system, defuse this demographic time-bomb? He notes that the French are having more children ("a clear sign of optimism," he jokes) and that there are plenty of people, women in particular, who could join the tax-paying workforce. In short, "I reject Malthusian visions of the economy."

A candidate for the bosses, therefore, and another for the workers? Not exactly. Both men, neck-and-neck in the opinion polls, know that they have to gain the middle ground to win. That is why Mr Chirac, to appeal to the left, stresses social "solidarity" and the environment. And it is why Mr Jospin, to avoid scaring the right, has said his programme is "not socialist", though he subtly amended the admission this week by saying "it is the programme of a socialist, a programme for France".

The trouble is, neither candidate has an idea how spacious the middle ground will be. Before they meet in the run-off vote on May 5th, they must first eliminate the lesser candidates in a first round on April 21st—and hope to gain those candidates' votes in the run-off. That means whoever comes third on April 21st has influence. In theory, it could be Jean-Marie Le Pen of the extreme-right; Jean-Pierre Chevènement, espousing "Republican values" that appeal to both left and right; or Arlette Laguiller, of the Trotskyite Workers' Struggle.

Neither candidate has an idea how spacious the middle ground will be

But in the second round, no one knows if Mr Le Pen's voters would settle for Mr Chirac, whom Mr Le Pen hates; or if Mr Chevènement's would go to his former colleague in government, Mr Jospin. As for Ms Laguiller, at the age of 62 now fighting her fifth and ever hopeless presidential campaign, the possibility is that she will gain the support of a tenth of the voters—and then advise these "protest" voters to abstain on May 5th. In other words, both Messrs Chirac and Jospin had better hope their brochures have an impact, not least because, as things stand, their backers on May 5th could find themselves outnumbered by those who vote for nobody.

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About sponsorship

Polish land

A most emotional issue

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An agreement on selling Polish land to EU citizens provokes controversy

WHAT is it about Poles and their land? The Polish prime minister, Leszek Miller, thought the deal his leftish government finally struck this month with the European Union on land sales to foreigners was the best his country could hope for. Yet many—perhaps most—Poles were outraged. Mr Miller had sold them out, they said; foreigners (meaning Germans) would descend “like crows” and pick the country apart. So what was Mr Miller's crime? He had managed to negotiate a 12-year transition for the sale of Polish land to EU nationals, five years longer than the government of any other applicant country has achieved. So why the big fuss?

Poles are attached to their land. Directly or indirectly, more than a quarter of them still earn their living from it; most city-dwellers retreat to it in the summer. In rural areas the feeling for land is intimate and sentimental, born of a folk culture that remembers not having any. Polish land is also much cheaper to buy than in neighbouring Germany. Even economically liberal Poles, who crave foreign investment in other spheres, are nervous about “foreigners speculating” on Polish fields.

Moreover, repeated invasions have made Poles jittery about anything to do with borders and territory. To Polish patriots, land is not so much a good as a heritage never to be betrayed. For many of them their role model is Slimak, a dimwitted peasant in a 19th-century novel by Boleslaw Prus. Slimak (literally, snail) is slow, incoherent, useless, but he knows one thing: not to sell his tiny plot to the Germans. The Slimak mentality helps explain why even the communists found it hard to collectivise Polish land after the second world war; by the time communism ended a decade ago, barely a fifth was farmed collectively or by the state, against 90% in other countries of the Warsaw Pact.

Fear of a foreign takeover is strongest in northern and western Poland, once part of Germany. Farms are bigger there, and more enticing than the postage-stamp smallholdings that spatter Poland's poor eastern parts that were once part of Russia. In 1945, Poland's borders moved westward. Expelled Germans in the west and north were replaced by Polish refugees from what is now Ukraine. These refugees and their children worry that Germans will come and buy back their property.

Are the fears justified? Not especially. The EU deal is designed to limit land purchases by outsiders and deter so-called “speculators”. Ageing Germans are no more likely to return to their ancestral homes in Poland than Poles are to Ukraine. German farmers seem uninterested in tilling poor Polish soil anyway, especially without subsidies. The few foreign (mostly Dutch) farmers who do lease land often fare badly; some have had equipment sabotaged, their houses vandalised by irate locals; high operating costs have deterred others. Besides, the nationalist view of Polish history is selective: 17th-century Polish kings invited in foreign farmers, especially Scots, with much success.

Mr Miller, who was born in a big mill town, sounds baffled by his countrymen's mystical attachment to the soil. Still, he is canny enough to realise that land sales will be an emotive issue in next year's referendum on EU membership, on which he has staked his political future. “A no vote would be a disaster,” he says. But it is exactly what the feral politicians of Poland's new far-right want. They have already made common cause on land sales, shouting and singing patriotic songs in parliament in defence of the soil. Mr Miller is coolly betting on the “good sense of ordinary Poles”. Given a stark choice between staying out of the EU or agreeing to sell their fields, he thinks most Poles will prove less sentimental.

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Portugal's general election

Mandate for an odd couple

Mar 21st 2002 | LISBON
From The Economist print edition

Portugal needs strong government but will probably get a weak coalition

AP

It's emotional becoming prime minister

THEY started the campaign well ahead, hoping for the overall majority that the outgoing Socialists had not managed in six years of power. By the time voting closed on March 17th, Jose Manuel Durao Barroso and his Social Democrats (who, confusingly, are Portugal's main party of the centre-right) were biting their nails. Mr Durao Barroso will be able to form the next government, but only just.

With only 102 seats out of 230, against the Socialists' 95 (and maybe two more for both parties once émigré votes are totted up), he will have to draw in the 14 of the populist People's Party, headed by Paulo Portas. This is a bitter pill. In the old days of Social Democrat power, Mr Portas, as a journalist, loved to damn the government. Mr Durao Barroso, its then foreign minister, came to his party's leadership in 1999 partly because its barons disliked its alliance in opposition with Mr Portas. And the populist leader far outshines Mr Durao Barroso as a personality.

But, when the alternative is yet another minority government, Mr Durao Barroso will probably have to grit his teeth and cosy up to Mr Portas. President Jorge Sampaio has said he is eager to avoid elections in a few months' time. And Mr Durao Barroso has echoed that, talking firmly of “stable and credible” government for the new parliament's four-year term.

How stable would the partnership be? On some things the two parties are close enough. Mr Durao Barroso campaigned promising to give the sluggish economy a “fiscal shock”: he would cut corporation tax, over time, from today's 28% to 20%, and the top rate of income tax from 40% to 35%. But can he afford it, with this year's budget deficit, as planned by the Socialists, near 2% of GDP? He will have to cut spending fast and hard, as he also promised; and Mr Portas—besides less immigration, more bashing of crime and drugs and the national anthem in schools—wants lower levels of the state pension boosted. The shock's benign effects will have to come through fast as well.

It may yet all happen. But the shock will be bound to hurt public employees, over-numerous, arguably over-paid and certainly well unionised. That, plus a narrow majority in parliament, is no ideal setting for a coalition dependent on a forceful and volatile junior partner. Do not bet on four years of stability—which is a pity, given the preceding years of weak government, and Portugal's plain need for a strong one.

Still, outsiders will hail one change already announced: Mr Durao Barroso will stamp on plans to replace Lisbon's wondrously convenient city-edge airport with a modern wonder at the back of beyond. And those ten football stadiums promised by the previous government for the Euro 2004 competition? No stopping them.

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About sponsorship

The EU summit on liberalisation

Energy and lethargy

Mar 21st 2002 | BARCELONA
From The Economist print edition

The bounty of Barcelona

Energy	Liberalised at last but only if you own a business. Domestic users must wait for further action
Galileo	Europe's satellite-positioning system nears blast off but at what cost?
Health	A European health-insurance card to be introduced
Financial services	All the laws to establish a single market in financial services to be adopted "as early as possible"
Languages	All European children to learn at least two foreign languages

Source: *The Economist*

Europe's quest for more liberal economies is slow and contradictory

THE European Union's Barcelona summit, which ended on March 16th, was played out against the usual backdrop of noisy "anti-globalisation" demonstrations and massive security. If nothing else, the demonstrations illustrated that economic liberalisation in Europe—the meeting's main topic—presents genuine political difficulties. Influential sections of public opinion continue to oppose anything that they imagine threatens "social Europe", the ideal of a cradle-to-grave welfare state.

In this climate of public opinion, it is not surprising that the outcome in Barcelona was modest. The totemic issue was opening up Europe's energy markets. The French government has fought hard to preserve a protected market at home for its state-owned national champion, Electricité de France (EDF). At Barcelona it made a well-flagged tactical retreat. The summiteers concluded that from 2004 industrial users across Europe would be able to choose from competing energy suppliers, which should account for "at least" 60% of the market.

Since Europe's energy market is worth *euro*350 billion ($309 billion) a year and affects just about every business, this is a breakthrough. But even the energy deal has disappointing aspects. Confining competition to business users makes it harder to show that economic liberalisation is the friend rather than the foe of the ordinary person. It also allows EDF to keep its monopoly in the most profitable chunk of the French market.

In other areas, especially to do with Europe's sticky labour markets, the EU is actually going backwards. The summiteers declared that "disincentives against taking up jobs" should be removed; 20m jobs should be created within the EU by 2010. But only three days after the Barcelona jamboree, the European Commission endorsed a new law that would give all temporary-agency workers the same rights as full-timers within six weeks of getting their feet under the desk. Six out of 20 commissioners did, unusually, vote against the measure—a blatant piece of re-regulation—but the social affairs commissoner, Anna Diamantopoulou, was unrepentant, indeed triumphant. A disgruntled liberaliser in the commission called the directive "an absolute disaster".

The summit's other achievements are still more fragile. Europe's leaders promised to increase spending on "research and development" from its current figure of 1.9% of GDP a year to 3%. But how will European politicians compel businesses to invest more in research? Nobody seems to know. And the one big research project agreed on at Barcelona, the Galileo satellite-positioning system, which is supposed to cost *euro*3.2 billion of public money, is of dubious commercial value, since the Europeans already enjoy free access to the Americans' GPS system. Edward Bannerman, head of economics at the Centre for European Reform, a Blairite think-tank, calls Galileo "the common agricultural policy in space."

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Italy

Murder and the labour market

Mar 21st 2002 | ROME
From The Economist print edition

The killing of a lawyer who sought reform could yet inspire it

AP

Brave Biagi

TERRORISM, presumably of a home-grown kind, has reared its awful head again in Italy. The shooting in Bologna on March 19th of Marco Biagi, a professor of labour law, as he was cycling home from work, has scotched hopes that the murder of public figures by extremists is a thing of the past. Mr Biagi was advising the minister of labour and had helped draft controversial legislation to loosen up Italy's rigidly encrusted employment rules.

In a newspaper article published the day he was killed, Mr Biagi wrote that, because Italy had Europe's most rigid labour market, it had no alternative to reform. In his polemic, he also reviled another sacred cow of Italy's trade unions, the country's extravagant pension system. The EU has suggested that the pensionable age should be raised by five years by 2010, a call which, wrote Mr Biagi, should awaken Italy to the problem of its ageing population and growing numbers of pensioners.

A wealth of figures bolsters the case for a root-and-branch overhaul of labour law and pensions. Italy's jobless rate is 9%. In the poor south, one person in five is looking for work. Most workers can retire on pensions in their 50s. Spending on pensions swallows up 14% of Italy's GDP.

In spite of all this, the employers' clubs, the trade unions and Silvio Berlusconi's coalition government of the right have been arguing ferociously for several months about an arcane section of a “workers' statute” enacted in 1970 known as Article 18. This requires employers to take back any worker whose dismissal has been deemed unjust by the courts. The trade unions were incensed by the government's decision to dish the article. Italy's three main labour groups jointly declared a general strike for next month. In the aftermath of Mr Biagi's murder, Mr Berlusconi urged the trade unions to call it off. The CGIL, most left-wing of the unions, was already limbering up for its own rally on March 23rd.

After last weekend's summit of EU leaders in Barcelona, Mr Berlusconi said that he was not scared of demonstrations. In his determination to tackle labour and pensions reform, he may seek to cast himself as Italy's Margaret Thatcher. He certainly raised the temperature by suggesting that everyone might eventually have to delay their retirement until 65.

Strangely enough, Mr Biagi's murder may help the government to enforce change. The trade unions, who have strongly condemned violence and are already worried that the murder may be used to pep up propaganda against them, have been thrown on the defensive. The interior minister says that the murderers probably belong to an offshoot of the Red Brigades, a far-left terrorist group active in the 1970s and 1980s.

In May 1999, Massimo D'Antona, a law professor who advised the minister of labour, then a politician of the left, was murdered in Rome. This latest murder is no less of a blow to Italian democracy.

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Serbia and Montenegro

Bye-bye, Yugoslavia?

Mar 21st 2002
From The Economist print edition

In a tricky deal, the old federation of Yugoslavia may cease to exist

ABOUT seven weeks ago, Javier Solana, the EU's foreign-policy chief, offered a deal to the authorities in Belgrade, capital of both Serbia and Yugoslavia. The western world would tell Montenegro, Serbia's sole partner in the rump Yugoslav federation, to shelve plans for independence. In return, Serbia would have to send more suspects indicted for war crimes to the UN's tribunal at The Hague.

One half of the bargain plopped into place on March 14th, when, after much arm-twisting, Montenegro's President Milo Djukanovic accepted a plan that would replace Yugoslavia with an even looser federation called simply Serbia and Montenegro. Yugoslavia would be history. The new union would have some weakish joint institutions, including a presidency, a parliament and five ministries, but each side would keep its own economic system: the new euro would continue to be Montenegro's currency, the shaky dinar Serbia's.

Smart economists in both republics doubt whether such a deal can work. Mr Djukanovic is stressing that a vote on independence can still be held in three years' time. Balkan-watching bigwigs in Brussels are relieved that talk of border changes in the region, which jangles nerves in Kosovo, Macedonia and even Bosnia, should now be put aside.

It is the other half of Mr Solana's bargain that looks even trickier, thanks to a murky happening in Belgrade. Hours after the federal deal was announced, Yugoslav military police nabbed Momcilo Perisic, a retired general who was also one of Serbia's deputy prime ministers, and an American diplomat, David Neighbor, at a Belgrade restaurant. The former was accused of giving the latter sensitive military data. Whatever the truth of that allegation, the incident was almost certainly part of the Yugoslav army's effort to block the flow of evidence to The Hague.

The United States got an apology from the Yugoslav government for the fact that its man was held incommunicado for 15 hours. But Vojislav Kostunica, who as federal president runs the army, insists there was “concrete evidence” against the general—an assertion that the president's rival, Serbia's prime minister, Zoran Djindjic, did not contradict.

The net result is a windfall for Mr Kostunica's more nationalistic camp. The authorities in Belgrade, be they Serbian or what may soon be deemed “Serbian-and-Montenegrin” (that is to say, ex-Yugoslav), now seem less likely to comply with America's demand for more suspects to be sent to The Hague by the end of March. And Mr Kostunica is better placed to bid for leadership of the Serbian republic, which will become the bigger prize as the federation fades.

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Charlemagne

A big-country directoire for Europe?

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Some influential Frenchmen rather like the idea, but other Europeans are doubtful

THESE days it is often rather lonely being French. Just think what has happened to France's place in the world since the end of the cold war. It is hard for today's Frenchmen, especially those of a Gaullist tint, not to feel that their country is getting squeezed out of far too many things. “It is feeling rather left out at the moment,” a senior British diplomat delicately puts it. “On every front, the French exception is under mortal attack,” is how a candidly worried French strategist describes his country's lot. And since last September 11th, matters from the French point of view have got progressively worse.

Think back a little more than a decade. France was an actor on the world stage that made the brilliant best of its attributes. As a cold warrior with nuclear weapons it sat comfily at the top table, alongside economically shaky Britain and muscle-bound gigantic America, ever quick to assert its individualism even in its handling of the Russians and Chinese and especially in places such as the Middle East or Africa where it had its own historical interests. Above all, it artfully moulded the burgeoning European Union to its own ends; in the eyes of the oft-jaundiced British, it simply ran the continental club. In a well-worn metaphor, France was the ever-agile rider astride post-war Europe's powerful but ploddingly obedient German horse.

How things have changed. A reunified Germany, much bigger and bouncier, has bucked off that rider. It has turned its gaze eastwards to the old Mitteleuropa, carting its capital from sleepy Rhine-side Bonn to beefy Prussian Berlin. Its chancellor actually pursues national interests without apologising for the past. Worse, for the nation-on-horseback that could nudge the European beast this way and that, a just-manageable western club of 12 has swollen remorselessly to 15 and within a couple of years could number 25. France is no longer truly Germany's equal. The post-war duo no longer drives Europe. France will certainly not have the main say when the club has nearly doubled in size.

And then, in the phrase of France's current foreign minister, Hubert Védrine, there is the new “hyperpower”, the United States, towering above seven lesser “great powers”, of which three have come to be deemed Europe's “big three”: France, Germany and Britain. After September 11th, the French elite, on left and right, rallied to the cause. “We are all Americans now,” declared the organ of the traditionally slightly anti-American French intelligentsia, *Le Monde*. But the new warmth has not lasted. “Never has European and French solidarity with America been so strong,” sighs a leading French diplomat. “But never has America consulted us less on issues affecting us so directly.” The French despair of America's apparent love of the unilateral.

The irony is that, while France's attitude to NATO has long been ambivalent for fear that it is a vehicle for American dominance, the Parisian strategists' mantra is now that “NATO is dying”—and something must be done to keep it alive. Europe, after all, may still sometimes need those “simplistic” Americans (Mr Védrine's word) to kick down the stable door when fire breaks out in places like the Balkans.

In any event, the two great new phenomena of the new millennium—an ever-more-powerful America and a widening Europe in which France is but one nation among many—surely require, so French and much of European thinking goes, a coherent European foreign policy. But how to make one? It is impossible enough forging agreement in the current club of 15. How much harder when there are 25 opinionated foreign ministers at the table. Hence the renewed mutterings, in Paris, of that post-Revolution, just-pre-Napoleonic term, *le Directoire*, meaning (in today's parlance) a governing board of big-country Europeans to run a policy abroad that could make America, among others, pause. In reality, Europe's leading trio often quietly and informally (a favourite word among European diplomats) set the foreign agenda. So why not, suggest some logically-minded French, make the body more formal and therefore punchier?

Not all of us loved Napoleon, you know

Because all the others, Danes and Dutch to the fore, would be understandably furious. Remember what is now known as the “great Downing Street dinner disaster” late last year, when Tony Blair arranged an intimate *soirée* with the “bigs” to hone their European world-view, and all the leading also-rans turned up barely invited, in high dudgeon, in mid-swig? Small-country European anger at being rolled over by the burly bigs has been rising sharply of late. The French are very often the first to be denounced by the smaller fry as “arrogant”.

Calm down, say the would-be *directeurs*. Spain, Italy and new-coming Poland would be in the new body, a “big six”. And, as in the UN's Security Council, a clutch of smalls could take turns to be in it too. Let's discuss it all in the grand convention being chaired by our old president, Valéry Giscard d'Estaing. We all agree, surely, that the EU's rotating six-month presidency has to go (imagine Malta running a 25-country Europe) and that Javier Solana's job as the EU's foreign-policy voice and Chris Patten's as the commission's must be merged, with Mr Solana's in the ascendant. (And, by the way, hasn't the Spaniard done well for European prestige in Macedonia and nearly-ex-Yugoslavia?)

The Germans, ever-sensitive to suspicions that they might become bullies again, are very coy about the idea. The British say they prefer “coalitions of the willing”, citing ad hoc groupings such as “the Quint” (Europe's big three, plus Italy and the United States), which ran policy towards Kosovo. And top Frenchmen, like Mr Védrine, accept that a formal *directoire*, though alluring, is diplomatically impossible for the time being.

But later? Things evolve. Enlarging Europe is a work in progress. A Euro-constitution is being drafted. America's war on terror has barely begun. And France, however the world changes, has always been adept at making the cockerel's crow heard.

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About sponsorship

Older workers

Early retirement? Don't even think about it

Mar 21st 2002
From The Economist print edition

Guardian

If older people are to stay in the workplace, employers will have to change their attitudes and practices

FOR the past 30 or so years, something peculiar has been happening. Decade by decade, life expectancy for older people has risen at unprecedented rates. Yet those older people have taken a double dividend by retiring earlier and earlier, stretching the start of effective retirement often to as early as 50. In turn, more and more younger workers have dreamt of retiring even earlier.

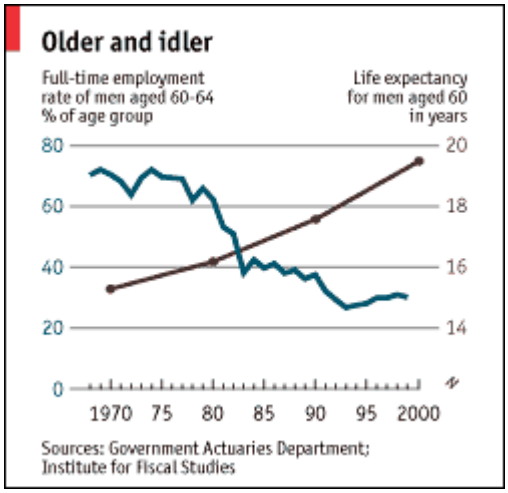
Not before time, there has been a rude awakening. Forget that dream: that is the message coming from pension providers. If you want to have a comfortable retirement then you will have to work longer. Earlier this month the Institute for Public Policy Research, the government's favourite think-tank, advocated raising the standard retirement age to 67.

Sheer common sense, you might think. But in practice there are three hurdles. Are older workers (often defined as over 50) up to the job? Do employers really want to hire and retain them? Do older people want to work anyway?

Physical strength clearly declines with age. So, too, do some cognitive abilities. Older workers perform worse than younger ones in tests of working memory and the ability to process complex new information rapidly, says Peter Warr of the Institute of Work Psychology at Sheffield University. However, declines in such capabilities are not crucial for most jobs, especially as physically strenuous ones become the exception in a service-based economy. What matters in today's workplace is the mix of skills, experience and character that individuals bring to bear. “Older workers are generally as good as younger workers,” says Mr Warr. And older employees show less absenteeism, lower turnover, fewer accidents, higher job satisfaction and more positive work values than younger workers, adds Amanda Griffiths, an occupational psychologist at Nottingham University.

The main link between age and work may operate through physical and mental health. There is a strong link between quitting work and poor health, says Costas Meghir of the Institute for Fiscal Studies. But this is paradoxical, to say the least. Rises in life expectancy surely signal better health, so why should so many more people be leaving the workplace now in their 50s and early 60s than was the case in the 1970s? A lot of evidence, not just in Britain but in many other developed countries, points to the fact that incapacity benefits have become an alternative pathway to early retirement for older people who lose their jobs and find it difficult to get new ones, argues Richard Blundell of University College, London.

That raises the second question: do employers want older workers, whatever their abilities? In the past 20 years they have often acted to the contrary. Whenever redundancies have been necessary, older workers have been the most vulnerable group. There is a widespread suspicion that employers do discriminate against people by age. The National Adult Learning Survey found in 1997 that almost four-fifths of people in their 50s and 60s agreed that “even if an older person studies to get qualifications, employers will usually choose a younger person”. According to the Employers' Forum on Age, two-thirds of information technology workers fear that they will be unable to get a job in IT once they pass 45.



However, age discrimination is going to be banned from 2006 under an EU directive. Even before the necessary legislation takes effect in Britain, there are signs that employers' attitudes are changing. Several now recognise that they were too hasty in winnowing out the ranks of older workers who were the repository for much corporate memory and wisdom. Nationwide Building Society, which has been pursuing a strategy of age diversity, has found that this policy pays by reducing turnover rates of staff. The saving in lower recruitment and training costs is £7m ($10m) a year, calculates Denise Walker, head of corporate personnel.

Quite apart from legislation, demographic pressures are forcing companies to appreciate the virtues of older workers. The labour force is ageing fast, as the postwar generation of baby-boomers matures. In the 1980s and early 1990s, employers held the upper hand, thanks to a surge of young workers into the labour market. But the number of people aged 25-34 is now falling sharply. In the past four years, the employment rate of older workers has risen faster than that for all workers.

One reason why older industrial workers were vulnerable to layoffs in the 1980s and 1990s is that the skills they had learnt for their trades lost value as the economy shifted away from industry to services. Because they had had less opportunity for formal education, many lacked the foundations in numeracy and literacy that would have allowed them to respond to the new requirements of the jobs market. By contrast, post-war generations which have benefited from more formal education should prove more adaptable.

But will older people want to carry on working even if employers now want them to? After all, it is quite rational for people to retire early, if they can afford to do so. High returns in the financial markets led to a rapid build-up in private pension wealth in the 1980s and 1990s. More and more people in their 50s found that it made sense to draw down this wealth earlier rather than later, argues Mr Blundell. Others were able to draw upon incapacity benefit if they found themselves unable to find jobs at acceptable wages.

However, these incentives now point to later rather than earlier retirement. The high returns on equities in the past two decades were “exceptional and future returns are bound to be much lower,” says Tim Bond of Barclays Capital. After two terrible years, the pension-fund surpluses that financed redundancies of older workers have been eroded. And the government has greatly tightened the rules allowing people to claim incapacity benefit.

For these reasons, Mr Blundell thinks that the age of early retirement is now ending. Even so, there is a lot to be done to make work more attractive for older people (which should in turn help all workers). Top of the list are demands for less stress, more flexibility in working arrangements including part-time and temporary work, and greater autonomy. These are more likely to be found in companies with flat, non-hierarchical structures. Just as workers need to adapt to the idea of later retirement, so too, do employers.

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Anatomy as art

Bodies beautiful

Mar 21st 2002
From The Economist print edition

Getting under your skin

British secretiveness about bodies informs the row about a new exhibition

JOHN DONNE, wrote his fellow poet T.S. Eliot, “knew the anguish of the marrow” and the “ague of the skeleton”. But that was only metaphorically. Visitors to “Body Worlds”, an exhibition newly opened in London (despite the objections of some MPs) will see the real thing. It consists of preserved body parts, sometimes in isolation, sometimes as part of the full Monty—whole bodies flayed and considerately splayed, leaving nothing to the imagination. For example, “The Rider” sits atop a flayed horse, holding his own brain in one hand and the horse's in the other.

As is customary in such cultural skirmishes, those shouting loudest (and inadvertently providing free publicity) hadn't seen the exhibition. But Gunther von Hagens, a German anatomist who invented “plastination”—the laborious process which ensures “The Rider” and his associates are so pliable and well-preserved, which Mr von Hagens modestly describes as “a new fate for the body”—is accustomed to controversy. His handiwork has been seen by more than 8m people, in five countries. In Germany, where, he says, corpses necessarily invoke historical guilt, he was described as “the new Mengele”. The British reaction has been conditioned by two national peculiarities: an extreme confusion about what constitutes art; and a special squeamishness about bodies.

Among his influences, Mr von Hagens cites Michelangelo, da Vinci, and other great anatomical artists who worked before the schism of art and science, and when operating theatres were just that. But he does not regard himself as an artist. Resemblances between his work and that of Rodin, Dali and others are, he says, coincidental—although the black fedora apparently plastinated to his head is a nod towards the anatomist's hat in a famous portrait by Rembrandt. The idea that his bodies might count as art, Mr von Hagens says, never cropped up until they left Japan for Europe. And whereas much modern art excites the intelligentsia but alienates the masses, his bodies do the reverse.

But it is especially understandable that they should be mistaken for art in London, where avant garde artists, to the bemusement of many onlookers, have long utilised the bodily fluids of various species in their work. In 1998, one of them was convicted of stealing body parts from the Royal College of Surgeons.

Rogue conceptual artists aside, corpses are no longer as familiar to most people in the West as they used to be. According to Mr von Hagens, no other country has a more secretive attitude towards death and the body than Britain, or a greater gulf between the carnal knowledge of medics and that of laymen. This theory is borne out by Britain's recent, macabre scandal over the illicit retention of dead children's organs by pathologists. Aggrieved parents from that episode are among those to have objected to “Body

Worlds”.

In his defence, Mr von Hagens—who divides his time between Kirgizstan, China and Heidelberg—argues that his work helps to dispel anxieties about bodies and death. Each day during the German showing, around five visitors to “Body Worlds” signed up to be plastinated (4,500 are on the waiting list so far). And after encountering an alcoholic liver and smoker's lung, Mr von Hagens claims, most emerge determined to live healthier lives; visitor feedback suggests that many resolve to donate their organs to science.

Coincidentally, while some politicians have been excoriating Mr von Hagens, Tom Watson, a Labour MP, has been drumming up support to change the rules governing organ donation. Britain has comparatively low donation rates, and a long and growing waiting list for transplants. Perhaps Mr von Hagens has a point.

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Crime

Don't panic

Mar 21st 2002
From The Economist print edition

Britain is not quite as dangerous a place as the home secretary says it is

Get article background

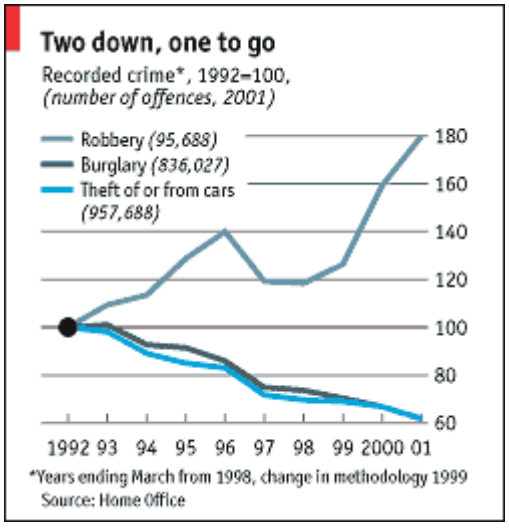
AP

I'm just a statistic

IN THE normal course of events, politicians can be relied upon to trumpet their successes, however inconsequential, and minimise their failures, however glaring. At the same time, they like to portray themselves as being on the same side as popular sentiment. Alas, these dual imperatives have created a dilemma for David Blunkett, the home secretary. The public, or at least the newspapers they read, have been berating Mr Blunkett for a perceived increase in lawlessness. Mr Blunkett has chosen to agree with them—even though the current anxiety exaggerates the true extent of crime in Britain.

The Home Office estimates that robbery will have risen by 29% in London in year to March 2002. Acknowledging this boom, and highlighting the role in it of 11-15-year-olds, Mr Blunkett last week convened a special summit to discuss what to do about it. He also announced a new initiative to tackle robbery in ten high-crime areas. So grave was the situation, he said, that this had been brought forward from its intended launch date in July (victims of street crime might reasonably ask why he had been intending to wait until the summer to do something about it).

The street-crime statistics reinforce the impression of anarchy created by a string of especially wanton muggings and car-jackings. But the palatable truth is that overall levels of crime are falling: robbery, while distressing, represents only a small fraction of the total. Over the last decade, the levels of car theft and burglary have declined (see chart). Criminologists speculate that improved home and vehicle security may have displaced some criminals on to the streets: the ecology of crime may be becoming more like that in some American cities, where robbery plays a proportionally bigger role than it does in Britain.



And the headline robbery statistics themselves may not be quite so mortifying as they seem. There has indeed been a particular explosion of robbery in the past year, which Barry Irving of the Police Foundation, a think-tank, thinks may be partly attributable to a squeeze in the casual labour market. But the longer-term trend is not necessarily evidence of a new plague of delinquency. As well as the closing of off-street opportunities, it reflects the advent of new on-street ones—specifically the temptation of mobile phones.

Robbery involving mobile phones is growing faster than robbery overall; robbery in which the phone is the only thing stolen is growing faster still. Home Office research suggests that if all robberies involving phones were disregarded, the overall figure might have fallen rather than risen in the last financial year. Many of these crimes are essentially a form of extortionate bullying, of a kind that previously would have gone un-reported. Of course, these are traumatic for the victims—but they bear little relation to the ultra-violence that preoccupies the tabloids.

But Mr Blunkett is right to worry about the growing participation of children. Mobile phone robbery is perpetrated by and against unusually young people; 11-15-year-olds represent a quarter of all robbery suspects in London, according to the latest figures. Commander Andy Baker, of the Metropolitan Police, says that, as in America, the profile of gang members in Britain is getting younger.

So something does need to be done. In the last couple of months, when the London street-crime boom has been brought under control, the Met has shown that diverting officers to deal with it can make a difference. But the underlying causes will be trickier to address. Locking up more teenagers is probably not the answer. School exclusions and truancy are part of the problem, but keeping disruptive pupils off the streets may not be compatible with raising standards in the classroom.

What, though, explains Mr Blunkett's unusual self-deprecation? One theory is that the hype about street crime is a form of public blackmail: the police, under pressure from the government, have used it to embarrass the home secretary. For his part, Mr Blunkett may calculate that such a frank admission will strengthen his bargaining position in the ongoing discussions about spending priorities. In his defence, he could argue, as he did last week, that “there's no point in telling people that things are getting better if they don't actually believe it”. Fear of crime is indeed important—but a responsible home secretary should be trying to moderate public anxiety, rather than encouraging it with talk of Armageddon.

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Criminal justice

Prison isn't working

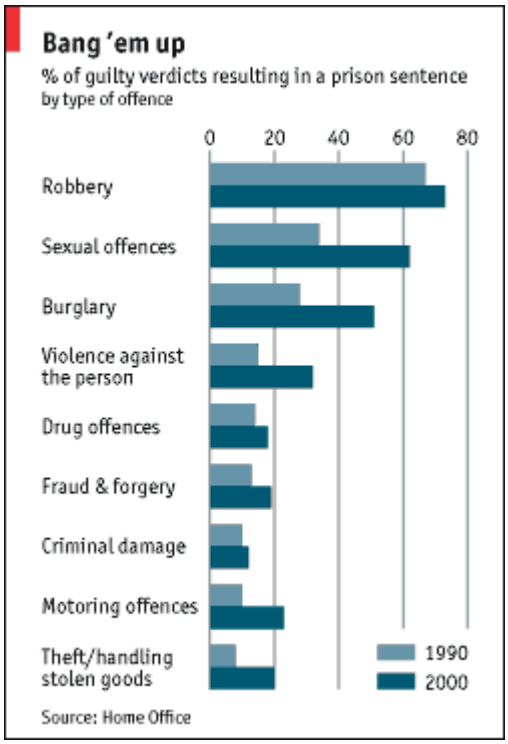
Mar 21st 2002
From The Economist print edition

Britain's desperately overcrowded prisons defeat the system's purpose

"PRISON works", the slogan adopted by Michael Howard, the former Conservative home secretary, and endorsed by his Labour successor, Jack Straw, is losing its appeal. Prisons are now so overcrowded that the current home secretary, David Blunkett, was forced this week to announce initiatives designed to reduce the strain. Ranging from the use of more electronic tagging and early release to new temporary buildings, the measures will ease the immediate crisis but they do not address the underlying problem.

Encouraged by the rhetoric of successive governments, and cheered on by the tabloids, the courts have adopted increasingly punitive sentencing policies (see chart). In the past decade, the prison population has risen by more than 50% to its current level of just over 70,000. England and Wales now have the highest imprisonment rate in Western Europe, and more prisoners serving life sentences than the rest of Western Europe put together.

The scale of the increase has caught ministers by surprise. At a time when Home Office statisticians had forecast that prison numbers would be static, the numbers have continued to rise, increasing by more than 5,000 in the past year alone. The result is that jails are bursting at the seams. Though 12,000 additional prison places have been provided over the past seven years at a cost of £1.28 billion, more than half of the 138 prisons in England and Wales are seriously overcrowded. Some local prisons, such as Shrewsbury, Leeds and Preston, have almost twice as many prisoners as they were designed to accommodate. The director-general of the prison service, Martin Narey, has told ministers, "I am not prepared to continue to apologise for failing prison after failing prison," and he said to the Prison Governors Conference, "I've had enough of trying to explain the very immorality of our treatment of some prisoners and the degradation of some establishments."



Overcrowding prevents prisons from doing their job properly. There are proven ways of reducing reoffending, but the first casualties of a service under strain are the very programmes which strive to do this. The Prison Service last year failed to meet more than half of the 18 targets the government has set it, such as those for work and training. Some prisoners say they are locked up for 23 hours a day. Targets for improving prisoners' basic skills in literacy and numeracy were also missed. Fewer than 10% of prisoners complete programmes, such as anger management, aimed at preventing reoffending. Just 15% of convicted sex offenders complete specialist treatment programmes.

Prisons are also supposed to help prisoners maintain stable relationships with their families. Academic research, sponsored by the Home Office, suggests that good family ties "can reduce a prisoner's risk of re-offending by six times". But overcrowding means more than half of all prisoners are held more than 50 miles away from where they were sentenced.

The cumulative result of these failings serves to undermine one of the key purposes of prisons. The Prison Service may be good at stopping prisoners escaping—the last escape by a category A prisoner was in 1995. But it has a poor record in preventing reoffending. Nearly 60% of prisoners discharged in 1997

were reconvicted within two years of release. For male young offenders, the reconviction rate is 76%. The real rate must be much higher because so few are caught, let alone convicted. Who says that prison works?

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Drugs

The prisoner's dilemma

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From The Economist print edition

Drug testing encourages prisoners to switch from soft to hard drugs

OVER the past decade, the number of people jailed for drug offences has trebled to 8,500. As more and more addicts have been imprisoned, drug-taking in prison has greatly increased. Research suggests that as many as one in five prisoners regularly takes illicit drugs. Many more use them occasionally. The Prison Service is trying a variety of counter-measures, including drug-free wings where prisoners who promise not to use drugs are given additional privileges. But stopping drugs being smuggled into prisons is impossible without draconian measures such as banning close-contact family visits.

One aspect of the Prison Service's drugs policy, random mandatory testing of up to 10% of the prison population each month, appears to be producing perverse results. The problem is that cannabis, the drug of choice for most prisoners, stays in the bloodstream and is thus detectable for up to a month. Heroin, by contrast, stays in the bloodstream for three days. A prisoner who tests positive for illegal drugs usually gets punished by having a certain number of days added on to his sentence. In the case of cannabis, this is usually about a week. For heroin and other hard drugs, it is about 28 days.

Prison warders say that, because the odds of being caught are so much lower with heroin, many prisoners are switching from soft to hard drugs to escape detection. Prison, says an academic who conducts research in prisons, is turning petty criminals into “smackheads”. Paul Cavadino, chief executive of NACRO, a prison reform group, says that some switching from cannabis to heroin is going on, but the scale is unclear.

The Prison Service claims that the proportion of prisoners using drugs has fallen from 30% three years ago to roughly 12% today. But that, of course, may just be because prisoners have switched to the hard drugs that help them avoid getting caught.

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Climate change

The green man

Mar 21st 2002
From The Economist print edition

Britain leads the world in tackling climate change

TONY BLAIR may be closer to George Bush than any other leader over the war against terrorism, but on another huge global issue—climate change—the two could hardly be further apart. Last year, Mr Bush ditched the Kyoto treaty, an international agreement on global warming that commits industrialised countries to sharp cuts in emissions of greenhouse gases (GHGs). He has since refused to produce any serious domestic climate policies. Mr Blair seems a tree-hugger in comparison. He is committed to the Kyoto treaty and says he will push it through Parliament this year.

Even more striking are his many climate policies. To help Britain meet its Kyoto target of reducing GHG emissions by 12.5% from their 1990 levels by the end of this decade, he has come up with a dizzying array of policies ranging from a new “climate change levy” (a form of energy tax) to renewable energy targets to more money for climate science.

And, on April 2nd, Mr Blair hopes to go where no one has gone before: GHG trading. Britain is about to become the first country with a full-scale scheme to trade emissions. Trading allows companies that can cut emissions at the lowest cost to do so; those that find it expensive to cut can buy “the right to pollute” as emissions credits. To kick-start the market, the government even held an auction on March 11th in which 34 companies made competing bids of GHG reductions to win a share of some £200m of government money.

Environmentalists point out that the green man's policies are not quite what they seem. According to the purists, there are two equally-efficient ways to reduce emissions of a pollutant like carbon dioxide (the chief GHG): an economy-wide tax on carbon emissions or a mandatory trading scheme with fixed emissions targets.

Mr Blair's plan appears to embrace both approaches, but fails to put teeth into either. His climate change levy, for example, is hardly an economy-wide tax: he has given so many businesses exemptions of up to 80% that it resembles Swiss cheese. Also, the GHG trading system is based on voluntary rather than mandatory targets, which is why the auction was needed to get companies interested.

But Britain's policies still add up to more than most countries'. As a civil servant says, “it is a softly-softly approach but we need to recognise political realities...besides, those theoretical ideas that look good on paper can be tricky in practice.” Mark Akhurst of BP, a progressive oil giant, says it is a good way to “learn by doing”. Somewhere between economic best practice and Mr Bush's worst practice, Mr Blair may have found a palatable “third way”.

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New public buildings

The price of national pride

Mar 21st 2002 | EDINBURGH
From The Economist print edition

The subtle art of getting round EU rules

THE new Scottish Parliament building is expected to be a great architectural wonder when it is finished, but for the present Scots are preoccupied with wonder at its cost. The original estimate was for £40m, but that was for a simple scheme on an easy-to-build-on site. The chosen design is complicated and the building is located on a difficult city centre site in Edinburgh. Two years ago, the estimate for the final bill had risen to £109m. Now it stands at £266m.

Scottish politicians are embarrassed. The cost overrun is partly their fault, for demanding more office space than was originally planned, and partly due to other factors, such as the refurbishment of an old building which has cost more than was expected. Still, the politicians are counting on the building being a source of great national pride, which is why everybody involved is keen that it should use lots of Scottish material.

This, it turns out, is a bit of a problem. The EU insists that such government building jobs should use the cheapest contractors and materials. Specifying local materials is strictly forbidden, because that might give local contractors an unfair advantage over builders from other EU countries. These rules are strict: the House of Commons' preference of a British-German firm over a cheaper American contractor for cladding on Portcullis House, a £233m office block for MPs, cost taxpayers £9.9m in compensation and legal fees.

So a lot of the oak being used in the Scottish parliament will be American timber cut to size in Thailand. But it seems that ways to bend the rules are being found. The granite for facing much of the building, for example, will be from Aberdeenshire, despite the fact that a Portuguese quarry offered cheaper granite. That's because, ahem, Scottish granite seems to be of a higher quality.

Similar problems are cropping up in Wales. The National Assembly pulled the plug on its new building when costs rose from £27m to about £40m. The architect, Lord Rogers, blamed political desires for expensive local materials; the politicians said his design was at fault. A cheaper builder is being sought.

Close by, work is now starting on the Wales Millennium Centre, a new home for Welsh National Opera. Naturally enough, people want it to resonate with Welshness. So the design calls for lots of steel and slate finishings. Using Welsh slate may be a bit of a problem—Spanish slate tends to be cheaper.

But the Welsh have devised ways round EU rules to give local timber a fighting chance of being used. Welsh wood is in short supply and, for some reason, seems to come in short planks. So lots of flooring has been designed to make use of different types of wood which, funnily enough, is to be laid in short planks.

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Bagehot

Snapping at his heels

Mar 21st 2002
From The Economist print edition

Tony Blair's critics are looking unusually bright-eyed and bushy-tailed

Get article background

AFTER three previous votes to ban fox-hunting, all by overwhelming majorities, this week's debate in the House of Commons should have been a rather desultory affair—a sort of parliamentary Groundhog Day. Not at all. Passions ran high. The anger of anti-hunting Labour MPs was as intense as ever. Most of it, however, was aimed not at the hunters, but at their own government. What infuriated them was the conviction that despite the certainty of another huge majority against hunting and the fact that the prime minister had himself rather ostentatiously voted for an outright ban, the government was looking for a compromise. Although it is not entirely clear what this "middle way", as it is known, would entail—probably the outlawing of some types of hunting with hounds, but the continuation of fox-hunting, albeit under tightly regulated conditions—it is as clear as a frosty country morning that whatever is cooked up will be regarded with revulsion by most Labour MPs. So why should Tony Blair be prepared to use up so much of his political capital to preserve something that he says he's against?

For what it is worth, Bagehot is not an enthusiastic supporter of the hunt, but he is even less enthusiastic about the trespass on individual freedoms that outlawing it entails. He also suspects, moreover, that despite Mr Blair's vote this week, the prime minister may have misgivings of a similar kind. The government's broader interest in the middle way probably has less to do with residual liberalism than with the desire to avoid some of the unpleasant consequences of an outright ban. It has no wish to see the inevitable armies of green Wellington boots marching on London, and worries that a campaign of civil disobedience could engulf the courts and the police. Mr Blair's instincts are always to try to reconcile opposites—that's what his creed of the "third way" is all about. Still, the balance of political risk for the prime minister may now have shifted.

Mutinous dogs

It's not just the grumpiness of Labour backbenchers during the hunting debate that should be of concern to Mr Blair. For a couple of weeks there has been a definite whiff in the air that isn't exactly of mutiny, but which is of more than just the usual truculence of those Labour MPs who never signed up for the Blair "project". Those to whom Downing Street refers as the "usual suspects" have a jauntiness about them that isn't explained by the arrival of spring. They sense that Mr Blair, never close to his party, is becoming dangerously remote from it.

When, on the eve of the Barcelona summit, John Monks, the head of the Trades Union Congress and the very model of a modern trade unionist, described the prime minister as "bloody stupid", it was a signal that something was up. In Mr Monks's eyes, Mr Blair has formed an axis of evil with Silvio Berlusconi to do down workers and replace "social Europe" with red-blooded American capitalism. Mr Monks's attack was informed by increasing anger among the unions about the way the government is going about reforming the public services—one moment assuring workers how valued they are, the next threatening them with the rigours of private management and reduced pension rights in the name of greater "flexibility". Although Mr Blair loftily dismissed the criticism as "mistaken", it's a fair assumption that a large number of Labour MPs were quietly cheering the TUC chief on.

The growing queasiness over Britain's role in the war against terrorism may cause even more trouble. Doubts about the campaign in Afghanistan were largely stilled by the sudden collapse of the Taliban and the Afghans' delight at being rid of them. But qualms are now flooding back. A parliamentary motion expressing "deep unease at the prospect that HMG might support US action against Iraq" has been

signed by 131 MPs—including about 40% of the Labour MPs who do not have government jobs. The signatories claim that the nods and winks they have had from people in government tell them that much of the cabinet is sceptical too. Iraq, in other words, would be “Tony's war”.

The prime minister says that people are protesting before they know what they're protesting about. But fears of foreign adventurism were strengthened this week by the surprise announcement that, at the Americans' request, Britain is dispatching a sizeable force of commandos to destroy al-Qaeda and Taliban fighters holed up in eastern Afghanistan. Although Britain's commitment to supporting the military effort in Afghanistan was always implicitly open-ended, that hasn't stopped a lot of people excitedly talking about Vietnam. But it isn't the scale of the commitment, so much as Mr Blair's readiness to do the bidding of President Bush, that arouses hostility in a Labour Party whose anti-Americanism runs deep.

Mr Blair is used to not being loved by his party, and it has never bothered him much. But two things have changed. Once the government had decided that establishing its credentials for prudent macroeconomic management was the overriding priority, its first term was remarkably uncontentious. The Labour Party understood that patience on public spending would be rewarded and, to its credit, it was extraordinarily patient. But now it is being asked to fight battles abroad that it has little stomach for, while being ordered to take on many of its natural supporters in the public-service unions at home.

Second, Labour has got used to being in power. When it could still remember its two decades in the cold, Mr Blair's electoral charm made him indispensable. But the government's massive second-term majority and the wretched state of the Tories have persuaded some MPs that they can fearlessly contemplate a future without him.

All of which means that the last thing the prime minister needs right now is a bruising tussle with his own MPs over an issue as slight as fox-hunting. Time for a stirrup-cup.

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Time travellers

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From The Economist print edition

The Gulf states have come a long way, fast. Now they need to think about where they are going, says Max Rodenbeck

DUBAI'S Internet City looks rather unreal, like an architect's model come alive. Mirrored façades gleam. Ever-blue sky glistens in reflecting pools. Smart-looking office workers mingle in open plazas. Yet the business conducted here is real enough. Two hundred firms employing 4,000 workers are installed already and another 100 are due to arrive this year, including big names such as Cisco, Sun and Oracle, following in the wake of Microsoft. By 2010, if the momentum keeps up as planned, the city's bold ambition is to host some 80,000 “knowledge professionals”, making it the IT hub of a region stretching from Bologna to Bangalore.

Until recently there was nothing here but desert, but three years ago Dubai's ruler, Sheikh Muhammad Bin Rashed al-Maktoum, thought up the idea of a fully serviced, tax-free IT village to complement his emirate's growing list of other attractions. These include the Media City taking shape next door, the yacht marina, the indoor ski slope, the tropical jungle and the giant, palm-tree shaped artificial island all under construction, and the string of sumptuous resorts along the nearby beach where 20 years ago there were only a few fishermen's huts.

Only yesterday

Here, as elsewhere in the Gulf, the pace of change has been breathtaking. In Dubai, where desalination plants now meet the country's voracious demand for water, old people remember filling tins from shallow wells outside the city and trundling them into town on donkeyback. The vast, low-lying sprawl of Riyadh, Saudi Arabia's capital, may soon be relieved by a pair of graceful skyscrapers, but some still recall the beggarwomen who used to squat in the dust by the gates of the king's mudbrick palace, whimpering for alms. Oman today is as orderly as Denmark, yet as recently as the 1960s lunatics were stumbling through the souks of its capital in leg-irons, and diminutive long-haired mountain men, naked to the waist and armed with axes, were roaming its remote interior. In what is now the asphalt jungle of Kuwait city, goats used to amble. And not so long ago the main landmark of Abu Dhabi, today a glittering Miami-scape of towers and boulevards set amidst lush parks, was a single scraggly acacia tree.

Numbers tell an equally dramatic tale. The population of the United Arab Emirates has increased 35-fold since 1950, and the area of the city of Riyadh has grown 100-fold. In Oman, electricity output has risen 670 times over the past 30 years, the number of telephones 420 times and the number of doctors

260 times. In Qatar, average incomes have grown 50-fold since 1960, and average wealth 200-fold.

“I grew up with camels,” says the Internet City's chief executive, Ahmed bin Byat, flicking back the folds of his crisp white headdress to sip his cappuccino in a glass-walled conference room. “My generation's been through a time machine that's left our parents in the old world and put our children in the new one.” The pace of change has been exciting, he says, but also stressful: “You constantly have to make decisions that will have an impact far into the future. You have to choose what to take with you and what to leave behind, because you can't take everything.”

Half a century ago, all six of the desert monarchies that make up the Gulf Co-operation Council (GCC) were wretchedly poor, thinly populated and so loosely governed they could barely claim the status of nations. All were catapulted into modernity by a gusher of oil, and left scrambling to find a way to manage their sudden riches. All have had to cope with the most wrenching change any part of the world has had to endure in living memory, including the fastest population growth, the most rapid urbanisation and some of the biggest tides of immigration.

By most measures they have done well. Since 1970 their governments have spent a combined total of $2 trillion to treble literacy levels to 75%, add 20 years to average life expectancy and create a world-class infrastructure. Education, once limited to a lucky few males living in large cities, or whose families could afford to send them abroad, is now universal and free. Health care and housing, subsidised by all six states, are generally of a high standard. And although the image of Arabs wallowing in wanton luxury persists abroad, Gulf societies, with some notable exceptions, are fairly egalitarian. Saudi Arabia's 5,000 princes and its great merchant families are indeed rich beyond the dreams of avarice, yet the kingdom as a whole has a per-head income little higher than Mexico's. Unlike Mexico, however, it has no slums or seriously deprived regions, no child malnutrition, practically no single-parent households and virtually no crime.

Thirty years ago an Egyptian diplomat could dismiss his Gulf neighbours as “tribes with flags”. This is no longer true: they are now countries with strong institutions and national identities. With minor exceptions, their borders—long a source of trouble, as Kuwaitis can attest—have been fixed for good. Their economies are the most dynamic in the region. Their business and government leaders are fairly sophisticated and outward-looking.

They need to be. The Gulf may never again see the kind of quantum leap in its fortunes that has transformed it over the past few decades, but it still faces the tough choices Mr bin Byat speaks of. Perhaps the toughest ones are yet to come. The period of nation-building is pretty much over. So, too, is the phase when oil wealth alone could make and keep the region prosperous, as well as insulate Gulf societies from the buffeting winds of globalisation.

This survey will argue that the Arab states of the Gulf, with few exceptions, have been slow to gear up for the problems ahead. This is not to say that they are unaware of what is needed. There is talk everywhere of shifting from quantity to quality in education, of employing more local and less imported labour, of freeing private industry and scaling down the role of the state, of opening up to foreign investment and of speeding regional integration. Several rulers are even giving political rights to their citizens, including women.

But more urgent action is needed. Unemployment has only just surfaced, but will balloon dangerously in coming years as populations continue to grow rapidly. Cradle-to-grave welfare systems will begin to come apart. With prospects for oil revenues flat for the indefinite future, diversification efforts must start now, while coffers are still fairly full. The chances of success would be much improved by an unconditional embrace of open markets and a big shift in government priorities, from planning and production

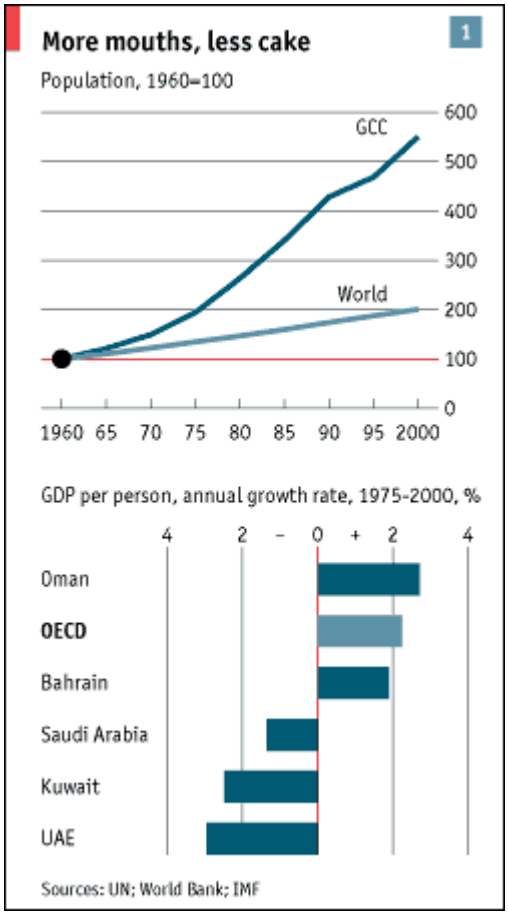
to regulation and arbitration.

Security is another concern. Huddling increasingly uncomfortably under an American umbrella, the GCC states have made little progress towards a joint defence. Given that they hold 45% of the world's known oil reserves, and are close to such emerging regional powers as India, Iran and China, they need to get organised.

Perhaps most difficult of all is the question, in Mr bin Byat's words, of “what to take with you” from the past. Gulf Arabs are proud of their traditions, and have tended to cast them in stone. Resistance to change need not be a bad thing, but the inflexibility of some Gulf societies holds back their potential for growth and for general well-being.

Political reform is vital—if not to sweep away the cosy patriarchies that currently siphon off so much of the region's vitality, then at least to render governments more effective, responsive and predictable. Women must be granted greater equality, whether conservatives like it or not. The new, more educated generation will not put up with the boredom and restrictions their mothers had to endure. And the economic argument against keeping half the workforce idle is conclusive.

And then there is the issue of Islam, swept to the fore by recent events. Since September's attacks on America, Muslims have been hurt by what they see as a wave of undeserved hostility. At the same time, though, few religious leaders in the Gulf have gone out of their way to advocate understanding and acceptance of other faiths and ways of life. Until they do, doubts will linger about the prospects of harmonious relations with that part of the world.



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Middle Earth

Mar 21st 2002
From The Economist print edition

Oil is big, but it is not the only reason to take the Gulf seriously

Contentious wealth

EVERY day some 16m barrels of oil leave the Gulf through the Strait of Hormuz. That is enough to fill a soft-drink can for everyone on earth, or to power every motor vehicle on the planet for 25 miles (40km). Gulf oil (including that from Iran and Iraq) accounts for 40% of global trade in the sticky stuff. More important, it makes up two-thirds of known deposits. Whereas at present production rates the rest of the world's oil reserves will last for a mere 25 years, the Gulf's will last for 100. In other words, the region's strategic importance is set to grow and grow.

Or at least so goes the conventional wisdom, which is usually rounded out with scary talk of unstable, spendthrift regimes and a lurking fundamentalist menace. Yet all those numbers come with caveats. A great deal of oil is consumed by the countries that produce it rather than traded, so in reality the Gulf accounts for less than a quarter of the world's daily consumption. As for reserves, the figures are as changeable as a mirage in the desert. The most comprehensive research available, conducted by the US Geological Survey (USGS World Petroleum Assessment 2000), refers to an “expected” total volume for global hydrocarbon deposits that is about double current known reserves. Using that figure, and throwing in natural gas along with oil (which makes sense because the use of gas is increasing far more rapidly), it appears that the Gulf contains a more moderate 30% or so of the planet's future fossil-fuel supplies, excluding coal, oil shale and everything else. Leaving out the two Gulf states that are not covered in this survey—Iran, with its immense gas holdings, and oil-rich Iraq—the remaining six between them hold something like 20% of world hydrocarbon reserves, not much more than Russia.

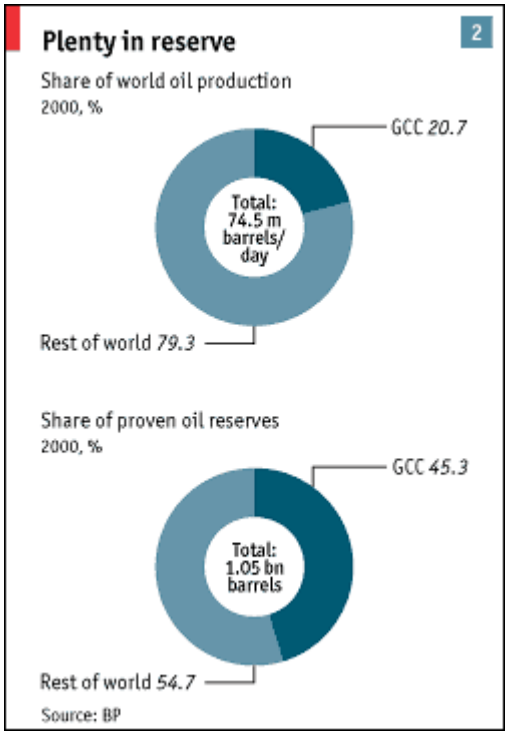
All the same, it is still a hefty chunk; enough, you might think, to keep the people living atop the wells in comfort for the foreseeable future. But you might be wrong. At present, the nations of the Gulf Co-operation Council have a combined national income roughly equal to Switzerland's, but a population which, at around 30m, is more than four times as big. It is also the fastest-growing on earth, having increased at nine times the Swiss rate over the past quarter-century. Meanwhile the region's share of world oil trade has fallen, as has the average price per barrel (amid much volatility). In real terms that price is not much higher now than when OPEC started pushing it up in 1973.

As a result, the income per person generated by GCC oil exports has been dwindling since the 1970s, precipitously in some countries: Saudi Arabia's GDP per head is now half of its 1980 peak. True, surging demand from America and Asia has recently boosted the Gulf's share of trade, but the medium-term outlook for oil prices remains weak. In the longer term, though, that could change. Twenty years from now, the rest of the world's reserves are likely to start declining fast. Combined with continued growth in oil consumption, this should create sustained upward pressure on prices. According to current predictions, by 2020 the Gulf will be supplying over half the world's oil needs. But by that time the Arab Gulf states' population will have doubled. And high oil prices will speed the search for alternatives. Who knows, in 20 years' time fuel cells and hydrogen power may have started to become commercial propositions.

GCC countries are doing their best to reduce their reliance on crude oil by building up sectors such as petrochemicals, banking

and tourism. Even Saudi Arabia, the region's lumbering giant, has seen the contribution of crude exports to its economy shrink from an estimated 70% in the 1970s to around 35% today. Bahrain and the semi-autonomous emirate of Dubai remain solidly prosperous with oil exports that account for less than 15% of their GDP. Kuwait, Qatar and Dubai's sister emirate of Abu Dhabi have such small populations relative to their hydrocarbon resources, and such hoards of overseas assets, that they can depend on oil to sustain them for some time to come, even at half today's prices.

And while the oil keeps flowing, the Arab Gulf remains a lucrative market for exporters of food, consumer goods, weapons and technologies associated with such things as power generation and waterworks. The region's merchandise imports add up to nearly the same as Russia's and India's combined. Its ports and airports, capitalising on their location between Europe and Asia, have gained a growing share of global shipping. Gulf Arabs play an important part in foreign markets, too, holding an estimated $1.3 trillion in overseas investments, including perhaps $400 billion-worth of American shares. And the 11m expatriate workers the region employs send home $25 billion in remittances every year, improving the economic lot of countries such as Egypt, Pakistan, Sri Lanka, Syria, India, Bangladesh and the Philippines.



An unquiet spot

Given the GCC countries' economic importance, there is reason to be concerned about their military weakness and their proximity to trouble. Some of the world's most bothersome hotspots are within Scud range: the Horn of Africa, Israel and Palestine, India and Pakistan, and Iraq. The closest neighbours are particularly worrying. Iraq's leader, Saddam Hussein, has invaded Iran, gassed Kurds, stamped on Kuwait, lobbed ordnance at the Saudis and kept hidden chemical weapons. Iran, despite reformist currents, behaves erratically, is armed with missiles, harbours nuclear ambitions, occupies two strategic islands that are claimed by the United Arab Emirates and has rejected offers to settle the matter in the World Court.

Nor is the Gulf Arabs' record of self-defence encouraging. Throughout the 1980s they lavished an average of 15% of GDP on arms, and billions more on financing Iraq's war against Iran. That did not stop their northern neighbour from trashing Kuwait in 1990. They had no option but to call for outside help.

Tighter budgets throughout the 1990s have reduced the GCC countries' defence spending to around 9% of GDP, but the region's armies remain heavy on hardware and light on skill and manpower. Plans to integrate their defence planning have produced feeble results, though the countries have recently committed themselves to enlarging their existing joint strike force from a puny 5,000 men to 20,000. They have made a poor fist of co-ordinating arms purchases, which has precluded standardisation of weapons for the foreseeable future, and they have failed to create unified air defences. Two decades after the formation of the Gulf Co-operation Council, all six members co-operate more closely with America on defence matters than with each other.

Given the overwhelming dominance of America's forces, that may not be surprising. There are occasional moans about American hegemony, but the superpower has tried to keep a low profile. The number of American troops in the Gulf—currently around 25,000—belies the scale of the commitment. The 5,000 American soldiers in Kuwait, for example, have access to stocks that could equip a combat force several times the size. A similar number of American troops man the Prince Sultan airbase near Riyadh, a fancy facility the size of the entire Kingdom of Bahrain—which itself houses American airbases, as well as the headquarters of America's 5th Fleet. Another great stash of American weaponry sits in Qatar, and the airbase facilities America enjoys there, as well as in Oman and in the UAE, could probably be upgraded should anything go wrong with the Prince Sultan base.

The Americans found access to an archipelago of Gulf facilities indispensable in their Afghan campaign, and have since added further to their presence in the region. All four of their armed services now have advance headquarters there, and are likely to stay as long as the Pentagon has its sights set on “regime change” in Iraq, despite rumblings about pulling out of Saudi Arabia that have echoed both in Congress

and in the Gulf. On Congress's side, the rumbles reflect disquiet about what has been perceived as a lame Saudi response to America's declaration of war on terror. It did not help that most of the September 11th hijackers, as well as their alleged paymaster, were Saudis. These concerns have revived older doubts about the nature of the Saudi regime, and particularly about its links with religious extremism.

The Saudis, for their part, have bristled at the suggestion that they might be indirectly responsible for an attack on their most important ally. Most of them think of Osama bin Laden as a heretic, which makes them all the more cross about being accused of fanaticism. Moreover, they are dismayed that the hostile noises coming from America, gleefully amplified in the local press, have actually increased the appeal of *jihad*-minded extremists.

The contrast between the kingdom's haughty secretiveness and America's preference for openness has always produced strains. Until the end of the cold war, a clear common interest helped to minimise the tension. But the past decade has seen growing Saudi ire at America's failure to “contain” Israel, and rising American irritation at the kingdom's friendliness towards Iran and Syria, which the Americans consider regional baddies. Crown Prince Abdullah, in effect Saudi Arabia's ruler, had even sent an anguished letter to George Bush only weeks before last September's attacks, decrying American indifference to the Palestinians and hinting that it was time to rethink the relationship.

Even so, the strength of American anger and Saudi indignation after September surprised both sides. The hurt will surely linger for some time. Healing it will require unusual tact from both, and there remains a danger that either American belligerence or Saudi obduracy could spark a real crisis. Yet America's long-term role in the region is not really in doubt. In private diwans, people do voice suspicions that the Americans are seeking control over the energy resources, not just of the Gulf but of the Caspian Sea and beyond. The region's leaders, however, recognise that what America wants is not physical possession but simply security—of oil supplies, trade routes and markets. That is something they can all agree on.

Saudi leaders may feel constrained about saying so at a time when America is flexing its muscles so openly, but the smaller Gulf states remain outspokenly pro-American. They share an ardent desire for “regime change” in Iraq, if not the will to risk bringing it about themselves. They quietly share hopes for a further cooling of Iran's revolutionary fervour. And they wholeheartedly agree on the need to bring *jihadist* militants to heel, even if they are wincing at the blunt instruments sometimes used for the task. Last but not least, the region's smaller monarchies appreciate America because they know that its presence keeps them safe from the ever-lurking fear that their Saudi big brother might try to push them around.

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People pressure

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From The Economist print edition

The world's emptiest quarter is filling up fast

Wasted resource

ON A WEEKDAY night this January, thousands of flag-waving youths packed Olaya Street, Riyadh's main shopping strip, to cheer a memorable Saudi victory in the GCC Cup football final. One car, rock music blaring from its stereo, squealed to a stop, blocking an intersection. The passengers leapt out, clambered on to the roof and danced wildly in front of the honking crowd. Having paralysed the traffic across half the city, they sped off before the police could catch them.

Such public exuberance was once unthinkable in the dourly conformist kingdom, but now young people there and in other Gulf states are increasingly willing to challenge authority. That does not make them rebels: respect for elders, for religious duty and for maintaining family bonds remain pre-eminent values, and premarital sex is generally out of the question. Yet demography is beginning to put pressure on ultra-conservative norms.

After all, 60% of the Gulf's native population is under the age of 25. With many more of its citizens in school than in the workforce, the region faces at least a generation of rocketing demand for employment. In every single GCC country the native workforce will double by 2020. In Saudi Arabia it will grow from 3.3m now to over 8m. The task of managing this surge would be daunting enough for any society, but is particularly forbidding in this region, for several reasons.

The first is that the Gulf suffers from a lopsided labour structure. This goes back to the 1970s, when ballooning oil incomes allowed governments to import millions of foreign workers and to dispense cosy jobs to the locals. The result is a two-tier workforce, with outsiders working mostly in the private sector and natives monopolising the state bureaucracy. In Kuwait, for example, 93% of the 200,000 native citizens who have jobs are employed by the government, whereas 98% of the 900,000 people working in the private sector are foreigners. The emirate's private firms are as productive as any. But within the government, claims one study, workers are worth only a quarter of what they get paid.

Head counts 3

Country	Total 2002* population '000	Population growth rate 1960-2000, % pa	Population under 15 years % of total†	Non-citizens % of total†	Expats as % of workforce†
Bahrain	650	3.6	28.8	40	64
Kuwait	2,300	4.9	33.5	64	81
Oman	2,400	3.9	44.5	26	55‡
Qatar	720	6.5	26.8	80	90‡
Saudi Arabia	23,000	4.1	43.4	27	55‡
UAE	3,300	8.8	26.7	82	90‡

Sources: Dubai Inc; Gulf Investment Corporation; US State Dept; UNDP *Forecast †Latest ‡Estimate

Similarly, in the education sector, 30 years spent keeping pace with soaring student numbers has taken a heavy toll on standards. The Saudi school system, for instance, today has to cope with 5m students, eight times more than in 1970. And many Gulf countries adapted their curricula from Egyptian models that are now thoroughly discredited. They continue to favour rote learning of “facts” intended to instill patriotism or religious values.

The system as a whole discourages intellectual curiosity. It channels students into acquiring prestige degrees rather than gaining marketable skills. Of the 120,000 graduates that Saudi universities produced between 1995 and 1999, only 10,000 had studied technical subjects such as architecture or engineering. They accounted for only 2% of the total number of Saudis entering the job market.

The party's over

Finding a future for the region's youth is not just a matter of numbers. The 1970s wave of excessive wealth has passed, but expectations remain high. Today's young people tend to assume that they will enjoy the same lifestyle as their parents, with a desk job and a state salary fat enough to support servants and idle wives, with cash left over for foreign travel and their childrens' costly weddings, as well as such perks as generous state housing loans.

That sort of government largesse is now out of the question. It is not that the pie is shrinking, but that it has to be cut into ever thinner slices. “This generation is beginning to realise they have missed the big party,” says an Omani anthropologist. “Their fathers had scholarships abroad, and came home to government salaries of $3,000 a month. These guys came out of our own universities, and have to hunt for work in the private sector, where starting rates now are more like $500.”

In Bahrain, Oman and Saudi Arabia, where oil income per citizen is relatively low, the frustrations are already evident. Overall unemployment may look low because of the high proportion of expatriates in the workforce, but the rate among local youths is rising alarmingly. On an unofficial count, it is over 20% among 18-30-year-olds in Oman, 14% in Bahrain and 15% among Saudi males (women barely register in the Saudi workforce). It is estimated that in the kingdom under half the 100,000 jobseekers entering the market every year currently find jobs.

In Bahrain, which was the first GCC country to strike oil and might be the first to run out, graduates already stage regular demonstrations to demand work. Kuwait, Qatar and the United Arab Emirates, with their tiny populations in relation to their oil riches, have so far been spared such unrest. But as Jassem al-Saadoun, a Kuwaiti economist, points out, “All that separates us from Bahrain is a little time.”

To ward off looming trouble, most Gulf countries have launched highly publicised campaigns to replace foreign workers with locals. There have been some successes. The native proportion of workers in private Omani companies, for example, has jumped from 10% to 20% since 1990. The “Saudisation” programme, which requires Saudi firms to raise the proportion of locals on their payrolls by five percentage points a year, has reduced the dominance of expatriates in sectors such as banking. And while many jobless youths do not bother to work because their families are wealthy and willing to keep them in comfort until “appropriate” positions arise, others have been forced into jobs once considered fit only for expatriates, such as driving taxis and working in petrol stations. This is the only way they can earn enough, these days, to go through the costly rites of marriage, home-building and child-rearing.

Yet anecdotal evidence suggests that the obstacles to employing locals remain formidable. Part of the problem is that although the Gulf has plenty of its own hard-driving high achievers, the years of easy money and state coddling have seriously weakened the work ethic. “I want to hire Saudis, but why would I hire someone who I know won't show up, won't care and can't be fired?” asks a Jeddah businessman. In Oman, some private firms resort to filling “Omanisation” quotas by hiring natives, then sending them home to let expats get on with the job. In Saudi Arabia, the government last year barred foreigners from working in the lucrative gold trade, then granted a flood of exceptions as dealers complained about a sudden surge in wage bills and a plunge in work quality. One international retail chain tried to please the Saudi authorities by hiring local sales staff. It received hundreds of applications, but after conducting large numbers of interviews turned away every single one of them for lack of qualifications or motivation.

The main obstacle to hiring locals, however, is simple economics. As an official in the Saudi Ministry of Planning explains, the classic principle is that wages should equal the marginal productivity of labour. “But here, since we've opened the gates to imported labour, we're talking about the marginal productivity of labour in Bangladesh.” In relatively poor Oman, many construction workers from the Indian subcontinent receive half the minimum legal wage for locals. With labour-exporting countries from India to Lebanon offering an unlimited supply of highly skilled, dedicated workers willing to accept low wages, the Gulf's employers naturally snap them up.

And it is not just businesses that think they are getting good value from expatriate workers, but private employers too. The estimated 3m domestic servants in the region, all foreigners, often endure conditions

equivalent to indentured servitude, with housing and food subtracted from salaries, no time off and no fringe benefits. Some of them start off indebted to employers who charge a “fee” for gaining visas and work permits. The luxury of having a docile, cheap and disposable workforce is hard to resist. Kuwait, in a feeble effort to narrow the wage gap and so encourage the hiring of Kuwaitis, decided to make employers pay for expatriates' health insurance (medical care for Kuwaitis being free). A revolt by householders forced the government to exempt domestic servants from the rule.

But Kuwait remains intent on trying to make wage levels converge. Another way of achieving the same aim would be to try to limit the number of expats. This would have the added advantage of stemming the outflow of remittances, which now drain the Gulf countries of some 10% of their GDP. Even government officials, however, recognise that this will take time. Besides, the trade in foreign labour is lucrative. Selling “sponsorships”, like letting out the property that foreigners are forbidden from owning in most GCC states, has come to be seen as a natural right of their citizens. And some of the region's peculiar traditions make it hard to do without foreign labour. For example, Saudi Arabia employs some 500,000 private chauffeurs for the simple reason that its women are not allowed to drive.

Bored to distraction

There is another reason why having lots of young, underemployed natives kicking their heels is not a good idea: boredom. This is especially acute in Saudi Arabia, where most women still languish at home, unable even to go shopping without a male chaperone. A small but growing number do work, albeit in carefully circumscribed trades and spaces. For example, the chief of econometrics in the Ministry of Planning leads a staff of 20 female statisticians by Internet and closed-circuit TV, because he is not allowed to be in the same room with them. And men, whatever their job, have to do without cinemas, bars or other distractions.

It is all very well to visit relatives, or to have family picnics in the desert, but not all the time. Small wonder that Internet chatrooms get roaring traffic. Small wonder, too, that some people get rowdy, whether that means singing football songs or running off to join the mujahideen. As a diplomat in the region says, “It's not just that boredom is demoralising. Added to the confusion between tradition and modernity, it makes people extremely, even dangerously, manipulable.”

Saudi Arabia is the most restrictive of them all: in the halting English words of a Syrian bellboy in Riyadh, “It is a very...dry country.” Kuwait has cinemas and puts few restrictions on women, and its citizens are wealthy enough to go abroad on holiday. Qatar and Oman permit alcohol, although their people bother less about it than their “teetotal” neighbours. Dubai and Bahrain, with their ladies' nights and go-go shows, take things a step further. But all across the Gulf, the amount of aimless milling and flirting that goes on in shopping malls suggests that people would gladly spend their time more usefully, if only they had something better to do.

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A pearl in the Indian diaspora

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Gulf Indians may lack citizenship, but many of them want for little else

YOU could be forgiven for finding the souks of Bur Dubai confusing. The lilting merchant patter, the scent of joss-sticks, the profusion of cashmeres, silks and cottons, and the polysyllabic splendour of shop names all evoke the shores of Gujarat rather than Arabia. The difference is that the names are spelled in English, the streets are spick and span, and the crowds look uniformly prosperous.

Not only look, but are. Many of Dubai's Indians, who make up the largest national group in the emirate (larger than locals), do work long hours for low wages, and scrimp for the day they can go home. Indeed, this applies to most of the Gulf's 3.5m non-resident Indians, or NRIs. Quite a few, however, have done very well indeed and sunk deep roots.

Maghanmal Pancholia's family, from the Sindhi city of Thatto, started trading pearls in the Gulf in the 1800s. By the 1920s, Mr Pancholia's father was running 30 dhows out of Sharjah. Life on the Trucial Coast then was too hard for wives and children, so his son finished school in India before joining the business in 1942. In those pioneering days before air conditioning, Mr Pancholia recalls, you had to buy murky well water for a rupee per tin, and filter it with cheesecloth. The only place to eat was a single kebab shop, the only way to get to the neighbouring emirate of Abu Dhabi was by sea, and a watchman with a gas lantern locked the souk's wooden gates after sunset.

As business prospered in the 50s, Mr Pancholia helped finance the construction of Dubai's first power plant and the dredging of the creek, a development that allowed the emirate to overtake its trading rivals. He recalls how Dubai's then ruler, Sheikh Rashid al-Maktoum, was so fond of the Indian *banian*, or merchants, that he visited their homes during the festival of *diwali* and made a point of serving vegetarian food.

In the plush boardroom of Dubai's India Club, a group of NRI businessmen chortle when Mr Pancholia, asked about his current line of business, says he sells watches. Mr Pancholia is too discreet to explain that he runs a business empire with a global reach in trade and finance, and is a big shareholder in several UAE banks. He is also revered in the Indian community as a generous philanthropist.

Just like home

His story is not unique. The Jashanmal department-store chain, with branches across the Gulf and sales in excess of $100m, started as a stationery shop serving British troops opened by Jhanglani Jashanmal in Basra, Iraq, in 1919. Khimji Ramdas, an Oman-based conglomerate with interests in trading, retailing, franchising, catering and manufacturing, was founded in 1870. The current partners, proud citizens of Oman, are 5th-generation descendants of Ramdas Thackersey, a native of Mandvi on the coast of Kutch.

In Dubai, one in 20 Asian households has a monthly income of more than $10,000. Indians here enjoy such ethnic amenities as Hindi-language radio and cinema, temples for most denominations, restaurants serving every variation of regional cuisine, cricket grounds, pageants and a full calendar of cultural events. Indeed, the tax-free emirate is so cosy that it has long served as a haven for the Indian underworld. Local police recently nabbed a Mafia don known as Farhan after he foolishly telephoned from Dubai to claim responsibility for a gun attack on the American Cultural Centre in Calcutta. In 1999, one Madhav Patel managed to defraud Dubai banks of $300m before vanishing.

One thing Dubai's NRIs do not enjoy, however, is citizenship. Nor have they been allowed to own property, at least until one luxury development offered foreigners 99-year leaseholds last year—most of which were snapped up by NRIs. But with business booming, no one is complaining. “Nationality has never been a handicap here,” says Mohan Valrani, a resident of 38 years who manages the local Shirawi

Group's 20-firm portfolio and chairs the India Club. “We've been treated well for 200 years. We appreciate operating in a really free economy, in a tolerant society where everyone's too busy to bother with religious stuff. Even between Indians and Pakistanis there is absolutely no tension here.”

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No taxation, no representation

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Absolute monarchy lives on in the Gulf. But for how long?

AP

SEEN from afar, the Gulf states look very much alike. They are all hot, dry, dripping with oil and ruled by conservative monarchs. Yet there are many more internal political differences among them than meets the eye.

It is true that, unlike in most of the world's surviving monarchies, rulers in this part of the world really do rule. Their families control every provincial governorship and senior military command. The prime ministers and the defence, foreign and interior ministers in all six countries belong to the ruling clans. In Oman, Sultan Qaboos himself officially holds every one of these posts, though lower-ranking ministers of state, all cousins of the sultan, are in charge of the day-to-day business. The sole, tiny exception is the United Arab Emirates, where the current minister of the interior happens to be a commoner, but more by accident than by egalitarian design.

The Gulf's ruling families are big. There are around 25,000 al-Sauds, though only 5,000 are princes, and only a hundred or so are senior princes. One in every 500 Kuwaitis is an al-Sabah. The same sort of ratio applies in most of the other states, although the al-Thanis of Qatar make up almost one in five of that country's citizens.

The sway of these families does not end with government. In the style of modern royals, the Gulf's princes and princesses, sheikhs and sheikhas are active patrons of sport, charity and the arts. What is less modern about the Gulf is the hazy distinction between government budgets and royal purses. The value of the stipends that each of the states pays to family members, including quite distant relatives, is mostly unknown. They also enjoy such perks as free travel on national airlines, free utilities and ownership of prime property.

Certainly, most of the Gulf's ruling clans have amassed large, and in some places truly colossal, fortunes. Part of this is simply luck: they happened to be in charge at a time when sudden oil wealth tipped the balance between the merchant classes and the sovereigns. But the big money has often come not directly from the oil wells but from private businessmen who seek the royals' patronage. “You can do business here without a partner from the family,” says an investor in one of the emirates. “But it sure smoothes the way.”

A plethora of princes

Country	Current head of state and start of reign	Effective ruler	Form of succession and next in line	Degree of democratisation
Kingdom of Bahrain	Sheikh Hamad bin Issa al-Khalifa, 1999	Same	Primogeniture; Crown Prince Sheikh Salman bin Hamad	Two houses, one elected, one appointed; elections by universal suffrage scheduled for autumn 2002
State of Kuwait	Sheikh Jaber al-Ahmad al-Sabah, 1979 (ailing)	Sheikh Sabah al-Ahmad al-Sabah, brother of the emir	Alternates between two branches of Sabah family; Crown Prince Sheikh Saad al-Abdullah (ailing)	Parliament elected by male citizens since 1965, but cabinet is appointed
Sultanate of Oman	Sultan Qaboos of Oman, 1970	Same	Male descendant from al-Said family, to be chosen by family council	Weak consultative assembly elected by limited suffrage
State of Qatar	Sheikh Hamad bin Khalifa al-Thani, 1995	Same	Ruling emir designates heir; Crown Prince Jassem bin Hamad al-Thani	Appointed consultative body, municipal elections by universal suffrage
Kingdom of Saudi Arabia	King Fahd, 1982 (ailing)	Crown Prince Abdullah	King appoints heir from Faisal branch of al-Saud family	Appointed consultative body
United Arab Emirates (Federal state composed of seven smaller emirates)	Sheikh Zayed bin Sultan al-Nahayan, emir of Abu Dhabi and president of UAE, 1966 (ailing)	Same	Crown Prince of Abu Dhabi, confirmed by other emirs; Sheikh Sultan bin Zayed al-Nahayan	Advisory national council, appointed by seven member emirates

Not much call for democracy

Most outsiders assume that the Gulf states are stifling autocracies. This is not altogether wrong, but needs to be tempered by an understanding of the region's unique history and social structure. To begin with, all the region's ruling families have held authority for a very long time. The al-Sauds trace their lineage back more than 30 generations, although they did not emerge as powerful princes in central Arabia until the mid-18th century. At different times they were allies of the Qawasim, who now rule the small emirates of Sharjah and Ras-al-Khaimah, and of the al-Sabahs of Kuwait, who gave refuge to the al- Sauds when they were briefly ousted from their lands in the 1880s. That debt was repaid during the Gulf war in 1990, when the al-Sabahs fled south from the invading Iraqis. Sultan Qaboos of Oman is the 12th descendant of the al-Busaid clan, whose founder controlled a vast Indian Ocean empire. The al-Khalifas of Bahrain conquered their pleasant island in 1783, leaving their poor cousins, the al-Thanis, to inherit Qatar, a desolate peninsula that turned out to hold more natural gas than all the rest of Arabia.

The Gulf's tribal, arch-patriarchal society bolsters royal rule. In every country a web of marriage alliances links ruling clans to other leading families. The al-Sauds, for example, are closely intermarried with the descendants of Muhammad Abd-al-Wahhab, an 18th-century religious reformer whose puritan version of Islam is sometimes called Wahhabism. Across the region, the tradition of the *majlis*, or open meeting between rulers and subjects, is held up as an effective form of popular representation. Outsiders may think that having a prince in charge of every Saudi province is feudal, but the al-Sauds argue that local *majlis* meetings keep the family attuned to the needs of their people. Sultan Qaboos, one of the most unfettered autocrats in the world, takes a caravan of ministers to a different region of Oman every spring where any petitioner can meet him face to face, seated on the floor of his tent, and see justice done on the spot.

Saudi Arabia and Oman are large countries with diverse native peoples, but the other Gulf monarchies are, in effect, city states where rulers and ruled are physically so close to each other that intermediaries are often unnecessary. Their citizens tend to identify more strongly with the sovereign than with the state.

Father figures

By and large, and in spite of the clumsy personality cults cranked up by the region's ubiquitous ministries of information, Gulf rulers are quite popular. Sheikh Zayed of Abu Dhabi, now 84, is revered at home and abroad, and not just for his fabled generosity and gruff desert wisdom. (He once told a French interviewer that he found it useful to meet his subjects personally, “Because our secret police don't get it right half the time.”) It was his vision that created the United Arab Emirates, and his charm that is largely responsible for holding the union together. Sultan Qaboos, too, is seen as the father of his nation, which Omanis readily admit was a medieval backwater before he overthrew his own father in 1970. Even Sheikh Jaber al-Sabah of Kuwait, though long-ailing, inarticulate and ineffectual, brings out spontaneous crowds of well-wishers on every return from a foreign sanatorium.

In spite of the clumsy personality cults cranked up by the region's ubiquitous ministries of information, Gulf rulers are quite popular

The institution of monarchy, with its centralised powers and long periods of reign, has stamped each Gulf state with the personality of its rulers. Oman is as neat and proper as might be expected of a place run by a Sandhurst graduate. The famously jovial demeanour of Dubai's Sheikh Rashid al-Maktoum, who ruled from 1958 to 1990, has left its mark in the emirate's laisser-faire attitude to business and social mores. The steely will and public-relations savvy of his son, Sheikh Muhammad, is the driving force behind its current boom. By contrast, the sense of drift evident in Kuwait, and until recently in Saudi Arabia, stems as much as anything from their rulers' lax attitudes and failing health.

Many of the Gulf's people recognise that it is not a good thing for their countries' fate to depend on rulers who may or may not be wise. Anxiety for the future is not much of a problem in countries with relatively young and dynamic leaders, such as Bahrain or Qatar, but it is a worry in several states where succession is a pressing issue. King Fahd of Saudi Arabia and Sheikh Jaber of Kuwait, both largely incapacitated by strokes, currently have able stand-ins. Yet Crown Prince Abdullah is already 78, and the Kuwaiti emir's brother, Sheikh Sabah, who runs day-to-day affairs, is also elderly and has 40 years of public service under his belt. In neither country is the path by which the next generation will come to power clearly defined. Saudi Arabia, in particular, looks set for a bout of brief reigns as the baton passes among the dozen or so remaining elderly sons of the kingdom's founder, Abdul Aziz ibn Saud. Unless,

that is, Abdullah assumes the throne soon and anoints a junior prince as his heir.

Plenty to be grateful for

Given all this uncertainty, the Gulf's citizens might be expected to want a bigger say for themselves. Pressure for democracy, however, is surprisingly weak. Aside from the weight of habit and history, the Gulf's people accept their rulers because they have been getting a pretty good deal. It is easy to say that this is only because oil wealth has made generous patronage possible. Yet it is also easy to understand that when your children's life expectancy is half as long again as your parents', as it is across the Gulf, and when the house that you live in was paid for mostly by the state, you tend to accept the status quo.

Another good thing about the Gulf is that its people pay no income tax. “I would love to pay tax,” sighs a would-be democrat in Saudi Arabia, “if only so I wouldn't have to pretend to be grateful all the time.”

“I would love to pay tax, if only so I wouldn't have to pretend to be grateful all the time”

All this means that demands to limit kingly powers are heard less frequently than calls for rulers to rein in their relatives, or at least to define their rights. In Saudi Arabia in particular, commoners point to continued royal extravagance despite straitened times. Businessmen complain that the country's plethora of princes elbow aside competitors. In an unprecedented sign of concern, Crown Prince Abdullah has tried to curtail princely commissions on public-works contracts.

Imposing family discipline is no easy task, however. The reforming emir of one state who had slashed his relatives' handsome stipends was forced to reinstate them when they threatened to revolt. In Bahrain, where the ruler, Sheikh Hamad al-Khalifa, changed his title from emir to king this year, observers say he was trying to sharpen the distinction between himself and his wider family so that he could trim their privileges at a later date.

More common than demands for democracy are calls for bolder, more responsive autocracy. “What we need is daring leadership that is receptive to criticism, accommodating to dissatisfaction, yet prepared to lose popularity,” says Abdullah Bishara, a former Kuwaiti diplomat and former secretary-general of the GCC.

This may sound odd coming from a noted liberal in a country that has by far the most deeply entrenched democratic institutions of any Gulf state. Yet Mr Bishara's opinion is the product of experience rather than of sentimental attraction to kingship. Like many Kuwaitis, he feels that the country's parliament, despite the healthy atmosphere of open debate it creates, has been more of a hindrance than a help to progress. Kuwait's 1962 constitution provides for an elected legislature, but for an executive government appointed by the ruler. This often results in a logjam. “Everything here gets kibitzed to death,” says a diplomat, citing a litany of important legislation, including a bill to grant women the vote, that has been blocked by parliamentary grandstanding.

It could be argued that the emirate's troubles could be solved by more democracy rather than less. Even so, Kuwait's experience has dampened enthusiasm for democracy elsewhere in the Gulf. Oddly enough, the biggest strides towards popular participation have been taken by the rulers themselves. Qatar, the first Arab country to have abolished its ministry of information, held municipal elections under universal suffrage in 1999, and its emir is thought to favour an elected legislature. Oman's Shura Council is directly elected, though its powers are purely advisory. Even in the rich, complacent United Arab Emirates there are whispers of reform.

The star reformer is Bahrain, a country that was wracked by violent unrest in the early 1990s, and whose Shia majority has long resented rule by a Sunni dynasty. Since coming to power in 1999, however, the then emir, now King Hamad, has emptied jails, freed the press, invited 1,000 exiles to come home, given them jobs and won over 98% approval for a charter of reform in a credible referendum. Local elections will be held this spring and national ones in the autumn. The result may not be a full transition to constitutional monarchy, because the king will still appoint a powerful upper legislative body, but Bahrainis seem optimistic that they have put their political troubles behind them.

Ripe for reform

Other Gulf leaders must envy the near-hero status that King Hamad has gained in such a short time. Yet perhaps Bahrain's example shows that some degree of trauma is needed to bring about dramatic change. The giant of the region, Saudi Arabia, may be in for just such a shaking. The kingdom is the Gulf's political laggard, with no representative institutions of any kind, a heavily restricted press and fearsome security services. There is no shortage of Saudis who want reform, including many within the ruling family. So far, any progress has been hobbled by the tangled matrix of interests at the centre of the Saudi power structure. But now, with oil prices slumping and demographic pressure mounting, the country finds itself squeezed as never before. Crown Prince Abdullah has himself spoken of a “suffocating crisis”. To enable them to escape from this predicament, the al-Sauds may have to secure a mandate from their people after all.

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The pen and the sword

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The complexities of Muslim identity

A STORY that takes pride of place in Saudi history books is how, one moonlit night in 1902, Saudi Arabia's founding father led 40 followers in a daring raid on Riyadh. It was Abdul Aziz ibn Saud's first step to avenging the rivals who had chased his clan from central Arabia. He was to succeed beyond his wildest dreams. But progress was slow at first until, at the urging of the puritan Wahhabi clerics who had been allied with the al-Saud family since the 18th century, Abdul Aziz sent out missionaries to preach *jihad* (holy war). Soon, bands of bedouin youths, determined to purge the faith of idolatry, began flocking to Abdul Aziz's banner. The new recruits, known as the *ikhwan*, or brothers, became his shock troops.

AP

A once-in-a-lifetime experience

Abdul Aziz won some territory by marriage, some by cunning, but most by the sword, with the ruthless *ikhwan* at the head of every cavalry charge. When the holy cities of Mecca and Medina fell in 1925, he found himself master of a poor and unwieldy territory stretching from the Gulf to the Red Sea. Abdul Aziz was astute enough to see that his power to control, let alone expand, the realm was already stretched. He turned his attention from conquest to state-building, and soon he, along with most of his subjects, began to tire of the *ikhwan*'s fanaticism. Pious though he was, Abdul Aziz chafed at their refusal to accept any form of "innovation", which they claimed to see even in such useful things as cars, telephones and electric power. They also disapproved of their leader's courting of foreign oil prospectors. Their intransigence, he feared, would dash his hopes of future wealth.

Worse still, some of the *ikhwan* refused to abandon *jihad*. Ignoring the borders that Abdul Aziz had settled with British-ruled Iraq, they regarded the country's Shia Muslim population as fair game. After all, Abdul Aziz's own great-great-grandfather had led a Wahhabi army to sack the Shia shrines of Najaf and Kerbala back in 1803. But when Britain's air force responded to *ikhwan* raids by bombing the invaders, Abdul Aziz decided he had had enough. In 1929, at a place called Sabila, 200 miles north of Riyadh, his loyalists used truck-mounted machine guns to blast the *ikhwan* into submission.

Unlike that daring moonlit raid on Riyadh, the encounter at Sabila does not get much play in Saudi schoolbooks. But it shows how hard it can be to get the genie of *jihad* back into its bottle. It also demonstrates that when sufficiently challenged, the al-Sauds are capable of some pretty effective recorking.

Saudi Arabia is the only modern Muslim state to have been created by *jihad*, and the only one based on an implicit alliance between the "men of the pen", or religious scholars, and the "men of the sword", an alliance symbolised by the Saudi national flag. The legacy of *jihad* has left an undercurrent of Wahhabi expansionism, which surfaces in the al-Sauds' generous funding of Islamic centres abroad, but also, fatefully, in ventures such as helping to liberate Afghanistan from Soviet rule.

Saudi Arabia is the only modern Muslim state to have been created by *jihad*

The limits to wordly power

The clerical alliance places heavy constraints on Saudi rulers. A revealing account of Abdul Aziz's court in the 1920s by Ameen Rihani, a Lebanese-American author, remains just as valid today: "The king may make a dozen treaties with infidel powers; he may call the people to...*jihad* as need be, he may grant a concession to an infidel corporation to exploit the oil and mineral wealth of the country, but he cannot

with immunity change a tittle in the Koranic law or directly abrogate, even modify, a religious custom."

This is why the kingdom remains the most formally conservative of Muslim countries. Most other Gulf Arabs, and many Saudis too, find the country's rules, particularly with regard to women, unduly rigid. They would agree that it suffers from a condition that Mr Rihani described as "Wahhabitis". Yet the kingdom has come a long way since the days when playing music or smoking cigarettes was punished by whipping. The Islamic code, or *sharia*, still governs civil and criminal law, but the need to engage with the outside world has allowed secular codes to creep into such spheres as commerce and banking. School textbooks may still exhort the faithful to shun infidels, citing narrow Wahhabi interpretations of tradition, and there are still provincial Saudis who will not respond to a Christian's greeting. But the vast majority of Saudis are perfectly at home in the wider world.

At least, so they thought until September 11th last year. The fact that the attacks on America were carried out in the name of Islam has shaken Muslims everywhere. In the Gulf, reaction to the event has taken two opposite directions. Perhaps predictably, it has provoked a backlash against *jihadist* extremism. Yet it has also roused Muslims' indignation at what they see as two injustices: that they are being collectively condemned for the actions of a few, and that the world is insensitive to Muslim suffering in places such as Palestine, Kashmir and Chechnya.

The backlash against extremists in the Gulf has taken several forms, some public, others less so. Shaking off initial timidity, governments across the region have strongly attacked the institutional props to *jihadist* groups such as Osama bin Laden's al-Qaeda. The hundreds of millions of dollars a year that once flowed unchecked to Islamic charities, some of which had links to extremists, are now carefully vetted. Every GCC country has introduced laws against money-laundering and frozen suspect bank accounts. Security forces have tightened controls on the movement of people, and in Saudi Arabia have arrested a number of suspects.

The backlash against extremists in the Gulf has taken several forms, some public, others less so

Perhaps more important, September 11th has shaken the Gulf out of its complacency about Muslim identity. The region's would-be modernisers have ended their long silence on the *jihadist* agenda. Since September, and particularly since the collapse of Taliban rule in Afghanistan, editorial columns in the Gulf have lambasted *jihadists* for leading the flock astray. They have openly questioned the logic of framing the answers to current problems in scriptural terms, and called for changing the intolerant tone of religious schooling. In public at least, liberals still only hint at the benefits of separating religion and state, but they are cheered by the trend towards limiting religious space.

Even Crown Prince Abdullah of Saudi Arabia, whose reputation for probity lends his words extra weight, recently gave a warning to mosque preachers that "exaggeration" in religion was making them "a target for those against Islam". This gentle princely circumlocution, however, also revealed how sensitive Saudi rulers are to the kingdom's conservative majority. Since September, the idea of powerful forces being ranged "against Islam" has gripped the region more than ever. This has less to do with sympathies towards Osama bin Laden, although his riches-to-rags tale continues to inspire some, than with exaggerated reports about western hostility towards Arabs. But then, with the less responsible American media describing Saudi Arabia as a "cancer", its rulers as "lacking in respect for life and humanity", and in one instance calling for an American takeover of oil fields, a certain prickliness might be expected.

Even Saudi liberals are dismayed by what they see as American heavy-handedness in pursuit of terrorism. "Bush's war is just not marketable here, with those ultimate double standards," says a Jeddah businessman, who says he used to "worship" the American constitution until it produced a president without experience of foreign affairs. "Why can't they see that our extremists are just like their Idaho militias? I admit their criticism of our schoolbooks is valid, but I doubt that Talmudic schools in Brooklyn are very polite about *goys*. And if we have crazy preachers, they have Oral Roberts and Jerry Falwell."

"If we have crazy preachers, they have Oral Roberts and Jerry Falwell"

A more common tack is to blame the West, and particularly America, for mistaking the symptoms (Islamist terrorism) for the disease (widespread Muslim anger about what many see as western contempt for their culture and aspirations). "It's not true that these people were influenced by Islamic teachings," asserts a junior Saudi prince. "They are like a cancer that needs something to feed on. If the West had addressed problems like Palestine, they would never have survived."

Such reactions suggest it will be a long time before Gulf societies dig to the roots of their discontent with

the world. Ordinary Muslims naturally take it for granted that their faith is good, and bridle at suggestions that there might be something wrong with it. The lack of a formal hierarchy in Sunni Islam, moreover, allows for conflicting interpretations, so that reformists are always exposed to conservative backbiting. And as often as not, those religious scholars who have gained wide enough respect to initiate change are the products of narrow training in scripture and have little experience of the world. They guard their independence jealously, yet their salaries are mostly paid by the state. If they were to adopt the more liberal line preferred by the region's rulers, they might be suspected of selling out.

In search of certainties

It does not help that the opportunities for open debate are limited. This is particularly true of Saudi Arabia, with its wary princes, timid media and total lack of representative institutions. Yet even in open-minded Kuwait, where the press and parliament are downright rowdy, Islamist politicians have clouded issues and hindered reform with their point-scoring, rabble-rousing tactics. Allied with tribal traditionalists, they have blocked government moves to grant women the vote, and forced Kuwait University to segregate classes. Together with members of parliament keen to protect the emirate's ruinously expensive welfare system, they have scuppered efforts to open up the economy.

Here, and elsewhere in the Gulf, a schism seems to be opening up. This is not so much about “western” versus “traditional” lifestyles, the most obvious sign of which is the contrast between lightly clad and heavily veiled shoppers in the mall. As often as not, young people in the Gulf are equally comfortable with either form of dress. There is even a trend towards mixing, say, a traditional white robe with a baseball cap, or a modest-looking headscarf with heavy make-up. In tolerant Dubai, whose commercial ethos and non-Muslim majority preclude heavy enforcement of religious rules, there is no tension to speak of. The Arab natives of the city uphold traditional ways not because they are made to but because they want to.

The deeper quandary is about where people turn for answers to life's questions. Should they struggle for practical, temporal solutions, or surrender to the infinitely detailed prescriptions that religious scholars are happy to provide? Struck by a tidal wave of change, Gulf Arabs are looking for certainties to cling to. At the same time the region's societies are proud of their resilience. “We are part of the world,” says Dr Ahmed Salah, an adviser to the Saudi Ministry of Planning who sports the regulation untrimmed beard of a true Wahhabi. “We cannot live alone. If we resist pressures, it is not because we are Islamic. We want to preserve our values like everyone else.”

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Meccanomics

Mar 21st 2002
From The Economist print edition

Profit from the prophet

BEFORE oil, religious tourism was Saudi Arabia's largest industry. It still ranks a distant second, generating annual revenues of perhaps $8 billion. Unlike oil, however, the “holy places hospitality trade”, as local entrepreneurs call it, is free of price volatility, and its underlying resource will not run out. It employs four times more workers than the oil industry. Best of all, it is growing faster than any other sector of the economy.

This may seem surprising, since there are clearly limits to the number of Muslims who can perform the *haj*, or pilgrimage to Mecca. This is a once-in-a-lifetime religious duty incumbent on all Muslims who can afford the journey. Over the past 30 years Saudi Arabia has invested $35 billion in improving facilities for pilgrims, but bottlenecks persist. Moving several million people, many of them elderly, along a four-day, 28km course of rituals within strict time limits is hard work.

Between 1950 and 1980 the number of pilgrims soared from 100,000 to 1m a year. Since then the Saudi authorities have imposed quotas on overseas pilgrims, which currently limit each country to one *haj* visa per 1,000 Muslim citizens. Even so, over the past decade the numbers have crept up by 3.5% a year. The number of overseas visitors expected this year was around 1.3m, in addition to 1.4m from within the kingdom.

The Saudis plan to cope with the continuing rise in demand by providing better infrastructure and, perhaps more important, by encouraging religious scholars to be more flexible. After a series of fatal accidents caused by overcrowding, for example, some Saudi scholars have extended the time allowed for the ritual stoning of pillars, one of the concluding rites of the *haj*.

Come, all ye faithful

The biggest growth, however, will come not from the *haj*, but from the non-obligatory *umra*, or lesser pilgrimage. Until recently, the Saudis issued *umra* visas only for the three months outside the *haj* season, banned their holders from travel outside the holy cities and restricted them to one trip a year and a maximum of two weeks' stay. All the same, rising incomes and cheaper, more frequent flights have caused *umra* travel to grow by 10% a year for the past decade. Some 750,000 Egyptians alone paid holiday visits to Mecca and Medina last year, a tenfold increase on 1991. Such visits are becoming increasingly fashionable even in distant countries such as Malaysia.

The Saudis have now opened the gates, allowing *umra* travel for nine months of the year. Pilgrims can come as often as they like, move throughout the country and stay for four weeks. *Umra* tour operators expect 2m visitors this year and are counting on a few years of 25-30% annual growth before the trend slows. Prince Sultan bin Salman, an ex-astronaut who heads the country's newly created tourist promotion agency, predicts a dizzying 34m visitors by 2020, and expects them to spend $23 billion. Half are likely to be *umra* travellers.

Mecca, where jumbled high-rise buildings already crowd the giant sanctuary, is getting ready for another boom. Land prices of $60,000 per square metre, many times more than in other expensive places such as Hong Kong, have done nothing to deter developers. Five colossal projects now in progress will alone add 50% to the accommodation available in the city by 2008.

On the Mountain of Omar, private developers plan to clear hundreds of old buildings to make way for 120 residential towers, each 20 storeys high, which will house a total of 100,000 people. On the hill of Ajyad, the trust that runs the Great Mosque recently demolished an 18th-century Ottoman fort. In its place will rise 11 apartment buildings, each with 40 storeys, and a 1,200-room five-star hotel. “Even after 1,422

years", notes Yasser al-Khouli, owner of a Jeddah software firm that devises "total solutions" for the pilgrimage industry, "the business around *haj* and *umra* is still virgin."

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Beyond oil

Mar 21st 2002
From The Economist print edition

The cure for oil addiction is known, but some find it unpalatable

The delights of Dubai

AFTER 20 years of driving taxis in Jeddah, Saudi Arabia's second city, Iqbal Kareem is going home to India. It's not worth the effort any more, he says. “They used to pay double or triple the meter. They didn't care. Now they bargain over half a riyal [about 15 US cents].”

Cabbies are great complainers the world over, yet Mr Kareem's declining fortune is not an isolated tale. Jeddah seems prosperous at first glance, but closer inspection reveals potholes, broken pavements and leaky drains. In summer, the lagoon bordering the central business district smells of sewage. A third of the city's 4m inhabitants rely on trucks to supply their drinking water.

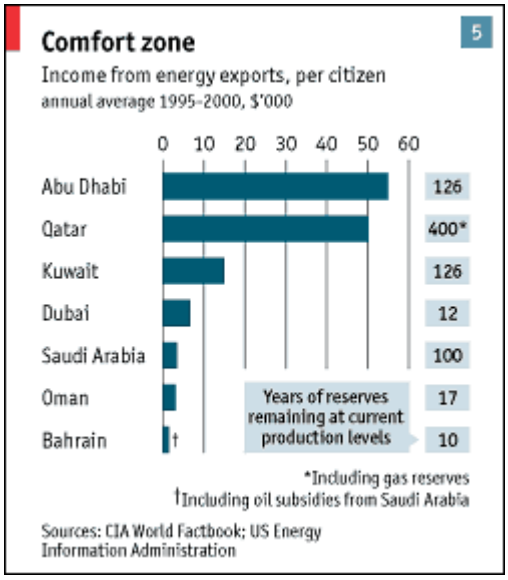
In 1980, Saudi Arabia was one of the richest countries in the world. Today, its economy supports twice as many people on an income not much higher in real terms. It remains the world's largest petroleum exporter, but it earns no more from oil than what America spends each year on cigarettes. Salaries alone drain 60% of the state budget, and domestic debt is bigger than GDP.

The kingdom is hardly poor, yet compared with its neighbours it is looking increasingly less comfortable. Its income per person is less than half that of upstart city-states such as Qatar or Abu Dhabi, where the shops far out-chic the kingdom's dowdy offerings, and where the average motor vehicle is one-third the age. Moreover, the poor parts of Saudi Arabia look scruffier even than the villages of Oman, a country that only 30 years ago had no paved roads outside the capital, and where income per head is only now nudging Saudi levels. Even the remotest hamlets of the mountainous sultanate are served by a mobile water distribution network more efficient than Jeddah's.

The kingdom's relative decline is not all its fault. The combined oil exports of all the GCC countries have dwindled from a peak of $150 billion in 1980 to an average of $80 billion in the 1990s. Most smaller Gulf states sell more oil per head than the Saudis, however, and have no need to extend costly infrastructure across a vast, largely empty hinterland. And most of them grew rich later, so they could learn from their big brother's mistakes. Their princely palaces are not so sumptuous, nor nearly so numerous. They did not splurge so lavishly on white elephants such as Riyadh's gargantuan $20 billion airport, a third of which has been mothballed since the 1980s. And although all Gulf countries followed the Saudi model of central planning and state capitalism, most of them have been faster to abandon it, quicker to diversify away from oil, and nimbler in attracting foreign investors.

It is also unfair to cast the kingdom as a couch potato. Saudi economists, businessmen and even government officials know quite well what is wrong, and what is needed to fix it. And indeed since a key speech by Crown Prince Abdullah in 1998, in which he plainly stated that the oil boom was over, economic reform has gathered pace. Among other things, Saudi Arabia has issued laws to protect foreign investment. It has slashed tariffs to 5% across the board. It has obliged the main state firms—the national airline, the power grid and the telephone operator—to make their accounts more transparent, and it has set up regulatory bodies ahead of privatisation. A slew of other streamlining legislation is in the pipeline. The kingdom is also moving ahead with a giant scheme to allow big foreign oil firms to develop its huge gas reserves.

Yet an enormous amount remains to be done. Economists say the country needs to sustain 6% annual growth just to keep unemployment in check, rather than the 1.5% achieved on average since 1980. Saudi officials reckon they must spend $200 billion on basic services alone over the next decade. Demand for electricity is set to grow by 250% in the next 20 years, and for desalinated water by 300%. With the government's budget chronically in the red even without such extra outlays, and the post-September oil-price slump adding further urgency, the only hope is to open up the economy, fast. “The country is at a critical juncture,” says the manager of a regional investment fund. “It can coast along without radical changes for only one or two years, maximum.”



To-do list

The prescription he has in mind is one that most outside analysts agree on. Privatisation needs to make rapid headway, and not only because private firms are more efficient. It is the best way of attracting back at least some of the $700 billion that wealthy Saudis have salted away abroad. Foreign investment in fields such as tourism, telecoms, utilities and financial services should be strongly encouraged. Taxes should be introduced, not just to reduce the state's debt, but to make revenues less dependent on volatile oil prices—or else the clerics who protest that anything other than a 2.5% “charity” tax is un-Islamic should be asked to pay for their free state schooling and health care.

The musty legal system needs an overhaul, too, whether the 700 religious judges who run it agree or not. This is not a question of tampering with Islamic law; it is a matter of standardising precedent, procedure and penalty so that citizens know where they stand. The cosy web of monopolies, exclusive agencies and commission-gathering gatekeepers must be dismantled, not only to squeeze profiteers but to create a transparent business climate that promotes trust.

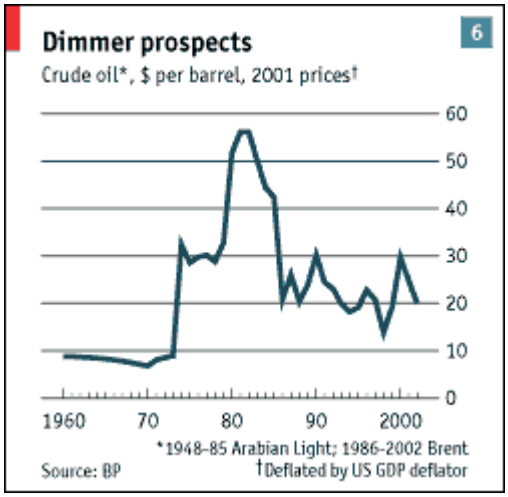
Social policies need to be updated, too. It seems reckless to shut away half the country's talent because it happens to be female. Simply allowing women to drive could save the kingdom the 1% of its income spent on imported chauffeurs. And the taboo against birth control needs to be dismantled, as it has been elsewhere in the Muslim world. No country can afford to meet runaway demand on limited resources forever.

Given the kingdom's political constraints and the power of its vested interests, Saudi businessmen recognise that little of this will happen in the near future. But they would like the government to make a bigger effort to explain the gravity of the situation, and to debate more openly what can be done about it. On this score, at least, progress is being made. Crown Prince Abdullah has been blunt about the challenges facing the country, and at a recent business forum in Jeddah Prince al-Waleed bin Talal, the billionaire chairman of Kingdom Holdings, an investment group, spoke of the “nightmare scenario” of oil prices at $10 a barrel.

To one degree or another, all the Gulf states suffer similar problems. Oddly enough, the need for reform is most urgent in sleek, smug Kuwait. A country with overseas savings, public and private, of some $200,000 per citizen might not seem in dire need of change, but Kuwait is performing far below its potential. Despite the country's financial clout, there is virtually nowhere to invest the money at home. About 90% of the government's revenue comes from oil, and 80% of the economy is run by the state. Yet an informal poll on privatisation found a majority against it, for fear it would cause the government's generous payroll to be trimmed.

So coddled are Kuwaitis that few bother even to pay their electricity bills. They owe the state utility an estimated $1 billion. The country is beginning to lose talent as the ambitious give up

and seek opportunities elsewhere. Even more worrying, the sclerosis affecting the bureaucracy has spread to the all-important oil sector. Technical incompetence, exacerbated by politicians handing out jobs for votes, was the underlying cause of a recent spate of deadly oil fires, according to most observers. And even Kuwait, say economists, cannot balance its budget when the oil price sinks below $22 a barrel.



Kuwait could learn a thing or two from its far poorer cousin, Oman. The sultanate has long recognised that it must make the most of its scant oil resources. It has spent frugally and made careful use of its natural advantages, such as its prime position astride important trade routes. The giant container port and free zone it has built at Salalah looks set to capture a growing share of the Indian Ocean transshipment business. And to make the best of its superb winter weather and miles of unspoilt coast, it has developed upmarket tourism rather than gone for the mass market. It has also moved ahead of its neighbours in privatising such assets as airports. Critics complain that Oman's government is complacent about its explosive population growth, its rigid labour laws and its turgid administration, but the bets are that it will still be a nice place to live when the oil dries up in 20 years' time.

Bahrain, too, has carved a niche for itself outside the oil business. This 700 sq km (270 square mile) archipelago manages some $85 billion in offshore banking assets. Financial institutions are attracted by a skilled workforce, good communications and a regulatory system considered the most effective in the region. The country long ago branched into industries such as aluminium refining, ship repair and petrochemicals. It also does a tidy business as a tourist destination for Saudis, who can drive across a causeway to soak up pleasures forbidden at home.

An open secret

But the Gulf's most dynamic and diverse economy, and the model that its neighbours increasingly turn to, is the tiny city-state of Dubai. It is so far ahead that it threatens to vacuum up much of the Gulf's free-floating business. A visit to the emirate's modest Economic Department helps to explain why. This is where businesses register, and it is clear that the place runs like a Swiss watch. So does Dubai's spanking new airport, from which it took this correspondent just seven minutes to exit, including passport control, luggage pick-up and customs. That was an improvement on the two hours once spent at Riyadh immigration, punctuated by police kicking casually at some Indian labourers who had fallen asleep in the queue.

“Dubai doesn't need to go through reform. It's already there,” beams the head of a government think-tank. The emirate is big on hype, but the view from his 45th-floor office bears out the boast: all swooshing highways, gleaming buildings and bustling ports in the distance. Dubai's population is growing at 5.5% a year, but the economy is growing faster still. Current construction projects include a vast new conference centre, a “Festival City” stretching along 4km of waterfront, a luxury housing estate for 150,000 residents, yet another giant air terminal, half a dozen skyscrapers and the same number of new 5-star hotels. Even this partial listing amounts to an investment of at least $15 billion, a sum equal to the emirate's entire GDP—and equal, too, to current orders for new aircraft by Dubai's booming flagship carrier, Emirates.

Naysayers claim that the place has overextended itself, that many of its vaunted projects are real-estate scams, and that the emirate can afford to spend so wildly only because the giant stores of oil in neighbouring Abu Dhabi, the anchor-state of the United Arab Emirates, offer a guarantee against default. So far, however, Dubai has lived up to the hype. Tourist numbers keep climbing. Competition from new ports, such as Oman's Salalah, has not stopped growth at Jebel Ali, the Dubai container terminal and free zone that all the others have copied. Even such unlikely-sounding events as the emirate's annual Shopping Festival seem to work. Last year it packed hotels to 90% capacity and generated $1.5 billion in extra sales.

Dubai's entrepreneurs like to attribute their prosperity to the no-nonsense business instincts of the ruling al-Maktoum family, whose current head, Sheikh Mohammad, takes advice from McKinsey and likes to be referred to as the emirate's CEO. “What's different here is that bright ideas get acted on immediately,” says an investment banker. With its nearby beaches, polyglot population and varied nightlife, the city is

also a congenial place to live. But the key to Dubai's success is being what its neighbours are not: open-minded, open-hearted and wide open for business.

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Bankruptcy

Up from the ashes

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Amid a global wave of business failures, American firms are more likely to get a second chance. Unfair competition, or a lesson for Europeans?

THROUGH European executives' eyes, American bankruptcies are perverse affairs. First, failed managers often hang on to the helm well after their firms have officially gone bust. After companies seek safe harbour under Chapter 11, America's famous insolvency law, banks swoop in to lend them even more money. Next, lawyers help the firm restructure older debts, giving bosses months or years to run their businesses interest-free. Failure, American style, is nice work if you can get it.

This is caricature, of course, but it is easy to understand why European managers might feel hard-done-by. In Europe, where moves are afoot to make life easier for troubled firms, such perks are much envied. Britain has toyed for years with plans to relax its insolvency rules, and is now close to doing so. The European Commission, too, will put up ideas for bankruptcy reform later this year.

For now, though, European executives can only look jealously at the likes of Covad, an American telecoms company, which recently emerged debt-free from a four-month stint in the bankruptcy courts. It was able to erase all of its $1.4 billion in debt in exchange for giving bondholders 15% of its equity. Creditors, management and shareholders agreed the deal outside of the court. Their trip into Chapter 11 was but a formality. Covad even picked up new finance along the way.

Now consider the travails of Carrier1 International, another telecoms firm, but based in Europe. It also ran into debt troubles last year, and creditors balked at management's first offer of a debt-for-equity swap. By the time the company came up with new terms, Europe's patchwork of national insolvency laws—some of which make directors personally liable merely for letting an insolvent firm trade—made it impossible to carry on. The company has now been forced into administration; its assets are being sold off.

More such collapses may be on the way. Earlier this month, Energis, a British telecoms company, failed to meet a debt payment. It is now scrambling to convince its creditors to work out a deal before the administrators step in. But European law generally gives creditors more power, and less incentive to strike a bargain, than American law, which favours borrowers (perhaps, it is said, because some of the founding fathers fled to the new world to escape their creditors). Energis has only one month after its default before it falls into the hands of administrators, who often sack senior managers and take a knife to assets.

Quite right, some would say, especially those who see Chapter 11 as a prop for basket cases. This has been true of America's airline business in the past, and arguably of its steel industry today. But most

American bankruptcies in this latest downturn have resulted in liquidation, as has historically been the case. Take Rhythms NetConnections, one of Covad's erstwhile American rivals. It filed for Chapter 11 at around the same time. But unlike its rival, it was deemed unsalvageable and was liquidated. More often than not, only those companies with a good chance of returning to health emerge from Chapter 11. That, say its supporters, shows that the law is doing exactly what it was intended to do.

Pre-packaged pain

Chapter 11 allows restructuring on three main fronts. First, companies caught out by disaster, legal liabilities or their own mismanagement can be forced to file for Chapter 11 out of desperation. But increasingly they can, like Covad, work out a deal in advance, and use the bankruptcy courts' tax and creditor-voting advantages—in some cases, approval is needed from only two-thirds of the lenders—to get the deal signed. Christopher Stuttard of BankruptcyData.com estimates that these so-called “pre-packaged” bankruptcies accounted for 8% of corporate failures in 2000 (by asset value), up from 4% in 1990. Third, Chapter 11's abundant case law also encourages out-of-court restructurings by letting borrowers and creditors know what to expect if they go to court.

While Britain is at the forefront in trying to emulate America's laws, much of continental Europe is still happy to rely on the state's heavy hand rather than on bankruptcy procedures. Holzmann, a German construction group, was saved from collapse two years ago by state aid. Now the company is in trouble again. As *The Economist* went to press, it was preparing to file for insolvency. If it is allowed to go bust this time, Holzmann would be Germany's biggest bankruptcy in decades—and the clearest sign yet that European governments are prepared to let capital markets work out business failures on their own.

Nobody expects radical changes to the European system to come quickly. Shagun Dubey, an insolvency expert with Ernst & Young, an accountancy firm, thinks that Europe will creep towards a hybrid of Chapter 11 and the current system, that would give managers of troubled companies less of a free hand than in America—frequent reporting to a trustee may become the norm, for instance.

The stigma of insolvency may be as big an obstacle as insolvency law itself. “Culturally, Britain is not sufficiently attuned to using insolvency...to return a restructured company to the hands of management,” says Mark Hyde, head of the insolvency practice at Clifford Chance, a law firm. Few banks in Europe are willing to lend to insolvent firms. Suppliers and customers, meanwhile, tend to treat bankruptcy as a scarlet letter.

Eurotunnel vision

For companies on both sides of the Atlantic, bankruptcy needs a clear goal. American firms are likely to fare far worse if they enter Chapter 11 groping for a recovery strategy, rather than having a plan in advance, says Peter Kaufman of the Gordian Group, an investment-banking boutique. In Europe, preparation for a financial solution is all the more important if default means a halt to trading. One hope is that Europe's less litigious culture might make companies and lenders more likely to plump for deals outside the courts. Britain, in particular, has some experience in this: Eurotunnel's reorganisation, for example. When the administrators step in, the European assets of only the biggest firms, such as Olympia & York, which built London's Canary Wharf, tend to be rescued.

Changes to practice are sure to come before changes in European law. Federal-Mogul, an American car-parts company, filed for bankruptcy in October, under both American and British insolvency laws. By co-ordinating its British bankruptcy with its Chapter 11 process, the company was able to keep its British businesses trading while in administration, with an eye to emerging as a single healthy company. This kind of approach, also used by firms such as ICO Global and PSINet, is a sign of things to come, says Jim Leshaw, a bankruptcy lawyer in Miami.

In the meantime, European firms need not feel too threatened by Chapter 11's advantages. When Chiquita, an American banana company, filed a pre-packaged bankruptcy last year, it was able to continue to compete with Fyffes, an Irish rival. But as Chiquita emerged from protection this week, its debt greatly reduced, a raft of companies lined up to make a bid. Rumoured to be among them was Fyffes, which, if it succeeds, might yet profit from America's forgiving ways.

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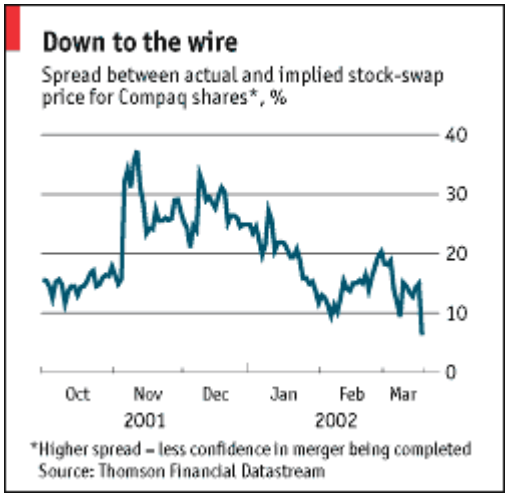
Hewlett-Packard and Compaq

Hanging chads, corporate style

Mar 21st 2002 | CUPERTINO, FLORIDA
From The Economist print edition

Carly Fiorina may have won the proxy battle, but not the merger war

Get article background



ONLY the infamous chads were missing. Otherwise, the vote by Hewlett-Packard (HP) shareholders on the firm's proposed merger with Compaq strongly recalled the tortured Florida vote in the 2000 presidential election. Shortly after a special shareholders meeting on March 19th, Carly Fiorina, HP's chief executive, declared victory with a "slim but sufficient" margin based on preliminary results. Walter Hewlett, son of one of the co-founders, who began the proxy fight against the deal, refused to concede defeat, describing the vote as "too close to call".

As *The Economist* went to press, it appeared that Ms Fiorina would indeed win, albeit by a tiny margin—perhaps only half a percentage point. But this could yet be reversed by the final count, perhaps several weeks away. The difficulty is determining shareholders' final and binding vote, since they were allowed to vote a second time if they changed their minds. What is more, either side could demand a recount or try to fight the result in court. (Mr Hewlett has ducked questions on this point.)

Even if Ms Fiorina wins the proxy battle, however, she will not have won the merger war. With so many of HP's shareholders having voted against the union, her seat will remain distinctly hot. Mr Hewlett has already announced his intention to remain "actively involved" in HP and would like to stay on the board. Calls for Ms Fiorina's resignation will come quickly if the merger is not executed well—particularly since an obvious successor has survived the controversy of recent months unscathed: Michael Capellas, Compaq's chief executive. On March 20th, an overwhelming majority of his company's shareholders voted for the merger.

After inundating shareholders with information about the merger, the management of the "New HP" will now focus more on educating its other constituents. The merged company plans, for instance, to embark on a worldwide campaign to inform customers about the product "roadmap" for the next three years.

Employees need convincing, too. Although Ms Fiorina insists that internal polls show the majority of HP's 88,000 employees worldwide in favour of the deal, there is undoubtedly strong opposition within the ranks. It will be hard to motivate Hewlettites to give their best for the new company. Some are sure to leave. "I love this company, but if the merger goes through, I won't be an employee...for much longer," one long-time staffer told Ms Fiorina at the shareholders meeting.

Merging with Compaq will not solve all of HP's strategic problems. Despite its breadth, the merged company's portfolio will have gaps that it must fill if it wants to become the IT-services and solutions powerhouse of Ms Fiorina's dreams. Software and outsourcing, for example, are areas in which "additional work needs to be done," she recently admitted.

And what if Mr Hewlett prevails? HP's future might then be even rockier. He thinks the company should invest more in its highly profitable printing and imaging business, then consider spinning this off. But what about HP's weaker businesses? Shorn of the printing part, their future would be bleak.

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Polish trade unions

Anti-social packages

Mar 21st 2002 | WARSAW
From The Economist print edition

The unions that defeated communism are now hobbling foreign investors

GONE are the days when Gdansk was Europe's hotbed of trade-union agitation. Yet even today this Polish port still suffers the odd rumble of discontent. In scenes reminiscent of the famed 1980 sit-ins at the Lenin shipyard that gave birth to Solidarity, Eastern Europe's first independent trade union, several hundred workers at nearby Stocznia Gdynia, Europe's sixth-largest shipbuilder, recently went on strike over wages and safety gear. Declaring the strike illegal, Gdynia's management sacked 120 of the protesters and said it would not tolerate further “lawlessness”.

Solidarity and Poland's other main union, the ex-communist All-Poland Alliance of Trade Unions (OPZZ), have long been a thorn in the side of company managers. Much of the unions' clout stems from Poland's political scene, which until last September's general election had a factory-floor look, with Solidarity and OPZZ well represented in parliament. While Solidarity has bowed out of politics—a thrashing in the election left it little choice—OPZZ's leaders are firmly entrenched. This is why the government is having a tough time pushing through labour-market reforms to halt a surge in joblessness, which could reach 20% by the end of this year.

The damage was done in the early post-communist years, when unions from big state-owned companies elbowed aside private business in helping to draw up Poland's labour code. The law coddles those with a job at the expense of those seeking one. The World Bank says the code is still “geared towards lifetime employment in large state enterprises” instead of towards the 75% of jobs in the private sector.

The unions have also stamped their authority on big privatisations by cajoling investors into signing “social packages”: contracts that compel acquirers to maintain employment levels for a specified period following a sale. The pacts also include one-off “privatisation bonuses” for all employees, generous wage increases and, often, special funds for a variety of causes. While such deals are not obligatory, the government expects investors to placate the unions before handing over the keys.

France Telecom knows a thing or two about social packages, having signed a mammoth one in 2000 when it bought into TPSA, Poland's telecoms giant. Solidarity, which represents a quarter of the operator's workforce, secured a ban on forced layoffs until February 2004. Tadeusz Najbauer, deputy head of Solidarity's telecoms unit, says the unions need the package as a bargaining tool to fight restructuring plans.

But it is Poland's assertive power-sector unions that have turned social-package negotiations into a fine art. A skilful bunch whose leaders keep in regular contact with other countries' unions, they are advised by expert lawyers and economists. “They even had a bloody psychologist,” says one irate foreign investor who recently bid for an electricity generator.

The power unions' proudest moment so far was wringing a ten-year moratorium on layoffs from Belgium's Tractebel in 2000 when it bought a stake in the Polaniec power plant. The ongoing sale of a cluster of eight distributors, known as the G8, could also entail a lavish package. The sell-off stalled late last year after two bidders failed to clinch a deal with the unions.

Poland's treasury minister has threatened to strip power privatisations of their social packages if the G8's unions block a deal, but few industry observers expect him to carry out the threat. Pity. With Poland's image among foreign investors at a low ebb following a series of stalled or cancelled sales, social packages—mercifully rare elsewhere in Central Europe—are a burden the country can ill afford.

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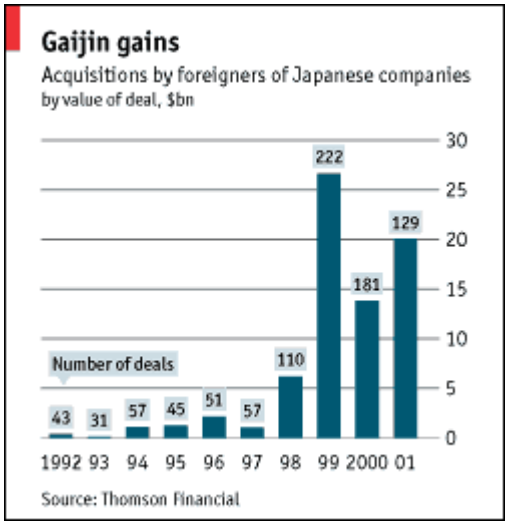
Japanese mergers

A chance for change

Mar 21st 2002 | TOKYO
From The Economist print edition

Foreigners are snapping up Japanese firms. But can they make a difference?

Get article background



FOREIGN investment has surged into Japan over the past three years, with American and European companies buying distressed companies at bargain prices. The value and number of such deals shot up in 1999 and has stayed high (see chart); last year, foreign buying accounted for almost a third of total mergers and acquisitions by value. Though cross-border mergers and alliances tend to be difficult, the tie-up in 1999 between Nissan Motor, a big, weak car maker, and Renault, a French rival, showed how successful they can be. Carlos Ghosn, Nissan's charismatic new president, turned the company around by cutting costs and shedding workers. Net profits for the year to March 31st are now expected to hit a record high, and the company is hiring back laid-off workers. Wal-Mart, an American retailing giant, will be hoping that its tie-up with Seiyu, Japan's fourth-largest supermarket chain, announced on March 14th, will be just as successful. Wal-Mart will buy a 6% stake, with an option to raise this to 66.7% by 2007.

Despite the recent influx of foreign capital, however, many Japanese business practices seem barely to have changed. Cross-border deal-making can sometimes be hampered by insular political interests. Last month, for instance, Snow Brand, a dairy-goods producer that is reeling from scandals involving tainted milk and mislabelled beef, admitted it needed a partner to survive. Politicians were so worried that a foreign company might shake up the well-protected dairy industry that they insisted Snow Brand choose a domestic partner instead.

For the most part, Japanese managers are happy to receive such orders. Most still prefer safe alliances with local rivals to link-ups with foreign managers bent on aggressive reform. Witness this week's combination of the semiconductor operations of Hitachi and Mitsubishi Electric. Under the deal's terms, up to 80% of the two companies' chip businesses will be folded into a 50:50 joint venture—a step forward in an industry crying out for consolidation, but hardly a radical solution. For most managers, selling to a foreign company is still considered a measure of last resort.

Exceptions are few and far between. One such is Osamu Nagayama, president of Chugai Pharmaceutical, a drug company that was taken over by Switzerland's Roche last December. Even before the merger, Mr Nagayama was famous for embracing western business practices, such as setting up an advisory board made up of foreign experts. But other healthy companies may not be quite ready to follow in Chugai's steps. Indeed, Mr Nagayama is considered a maverick in Japan's conservative pharmaceutical industry.

Still, when Japanese companies copy foreign reforms, the consequences can be surprisingly far-reaching. Take Nissan's decision to slash procurement costs, by cutting back on the number of its steel suppliers and making bulk purchases. Other car makers quickly followed suit, as did consumer-electronics companies, such as Toshiba and Matsushita Electric. This, says Conny Jamieson, steel analyst at UBS Warburg, helped to trigger sharp falls in steel prices. Steel makers' profits tumbled last year, forcing the industry into its first bout of real restructuring—including a merger between two giants, NKK and Kawasaki Steel—in more than 30 years.

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Beleaguered French bosses

All together now

Mar 21st 2002 | PARIS
From The Economist print edition

Is there something wrong with France's business culture?

Reuters

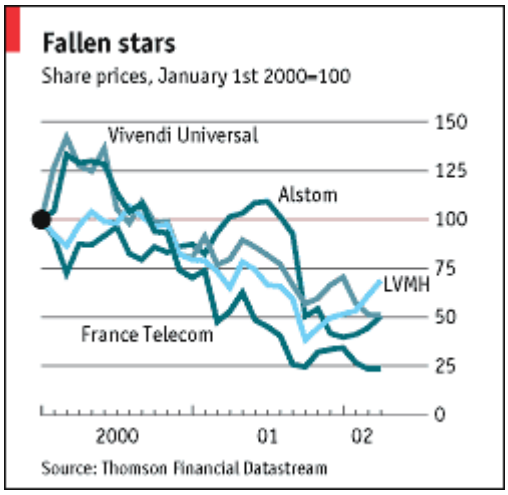
Messier tries to explain

NOT so long ago, France could look proudly on a crop of business leaders who had risen to the top of their industries. Think, for instance, of Jean-Marie Messier, who transformed a water company into Vivendi Universal, a media giant big enough to scrap with Rupert Murdoch; or Bernard Arnault and François Pinault, who respectively own LVMH and Pinault-Printemps-Redoute, two giant luxury-goods groups. Think, too, of Michel Bon, who turned France Telecom from a sleepy monopoly into one of its industry's most aggressive competitors.

How different things seem today. The reputations of these—and other—French bosses are in tatters. On March 21st, the once-fêted Mr Bon announced annual results that capped a miserable decline: a loss of *euro*8.3 billion ($7.4 billion), caused by a write-down of investments made during the telecoms bubble. France Telecom is burdened with some *euro*61 billion of debt. Its relationship with MobilCom, a German telecoms company in which it holds a 28.5% stake, is near to collapse. Mr Bon is also said to be considering a retreat from Wind, a mobile-phone venture in Italy, in order to raise cash.

To be fair to Mr Bon, his is not the only big European telecoms group in trouble. On March 18th, Deutsche Telekom cut its dividend and said it would miss previously announced debt-reduction targets. Ron Sommer, its chief executive, is about as unpopular in Germany as Mr Bon is in France. Shareholder groups accuse Mr Sommer of damaging Germany's nascent equity culture by mismanaging Deutsche Telekom, which dominates its domestic stockmarket.

But Mr Bon is especially vulnerable, as he can be sacked by the politicians who control France Telecom via the state's 55.5% stake. There is already talk in Paris of a scandal over the government's negligence in monitoring Mr Bon's acquisition spree at a time when he was also sacking thousands of workers. Once France's presidential and parliamentary elections are out of the way, in early summer, Mr Bon could face the chop.



Other French managers are doing their best to make Mr Bon's troubles seem less exceptional. In early March, Mr Messier presided over the largest annual loss in French corporate history when Vivendi Universal unveiled a *euro*13.6 billion deficit for 2001, caused by a vast acquisition-related write-off. Mr Messier showed signs of feeling the pressure when he claimed, bizarrely, not to have destroyed shareholder value because he had paid for deals in shares rather than cash.

Messrs Arnault and Pinault are also struggling with their empires and have seen their share prices tumble. LVMH has suffered from a series of management defections amid increasing criticism of Mr Arnault's autocratic management style. Mr Pinault's flagship company is struggling with big debts that will probably force it to restructure.

The crisis in French management is not limited to these headline-grabbing names. Pierre Bilger has

presided over a sharp decline at Alstom, a big engineering group, while Serge Tchuruk has led Alcatel, a telecoms-equipment maker, from bad to worse. Small wonder that wags talk of well-regarded executives, such as Jean-Pierre Garnier of GlaxoSmithKline (see article) or Jean-Martin Folz of PSA Peugeot Citroën, becoming an endangered species.

Surely this malaise is down to sickly world markets rather than uniquely French factors? Not entirely. French bosses are particularly cosy with each other, and this breeds introspection. A symptom is the tendency for top managers to sit on each other's boards. Mr Messier sits on Mr Arnault's, and Mr Arnault sits on Mr Messier's. The Vivendi boss sits on Alcatel's board, while Mr Tchuruk is a director of Vivendi and three other big firms.

But perhaps the mass collapse of managerial reputations also reflects French ambivalence towards big business. Suspicion of globalisation and Anglo-Saxon business practices, such as stock options, has risen since Enron's implosion. Further, tough market conditions everywhere have led to a reassessment of the extraordinary praise heaped on top managers in the good times. In France, critics of capitalism have been only too glad to make the most of their opportunity.

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South African alcohol

Grand slammers

Mar 21st 2002 | JOHANNESBURG
From The Economist print edition

Gesondheid! South Africa's booze exports are booming

SLAM a glass to celebrate. Agave Distillers, a drinks producer in Graaff-Reinet, a dusty town in South Africa's Karoo desert, is making merry after exporting 100,000 litres of agave spirit, also known as tequila, last year. That is a dribble compared with the many millions of litres produced in Mexico, but prospects look good because the agave plant, which flourishes in South Africa, has been blighted by disease across the Atlantic. Shortages have caused agave prices to rocket.

Agave Distillers is not alone. South African Breweries produces two-thirds of Africa's beer, and is big in developing countries—it is now China's number two brewer. But wine is the most important export tipple. A recent deal struck with the European Union lets South Africa export 42m litres to the EU duty-free each year. In return, local producers may not use established names, such as sherry and champagne, just as Mexico prevents Agave Distillers using the name tequila.

More foreign sales would top an extremely successful decade for South Africa's booze companies. Since 1992 their exports, mostly wine, have grown almost eightfold, from 22m litres to 174m litres in 2001.

The British and the Dutch are the keenest buyers. Americans and other Europeans have traditionally been more wary of African wine, but are warming to it—one reason why total exports of alcohol rose by 26% last year alone. A third of South Africa's vineyards have been replanted to yield more lucrative grapes in the past few years. But the country's greatest sales novelty may come from black viniculturalists, who are moving into the white-run world of wine. For those who tire of reds, whites and rosés, South Africa offers a fourth choice: a politically correct bottle of “black”.

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Movies and the Internet

Napster all over again?

Mar 21st 2002
From The Economist print edition

Hollywood feels threatened by Internet file-sharing services

Coming soon to a computer near you

THE file-swapping of recorded music on the Internet has already sent the music industry into a spin. Now it is Hollywood's turn to take fright. At its peak in February 2001, 2.8 billion music files were downloaded each month through Napster alone. The sharing of files containing pirated movies may still be in its infancy, but 300,000-500,000 feature films are already being downloaded daily, according to Viant, a consultancy.

This activity is set to grow thanks to three factors: the spread of broadband connections; the use of new compression formats that have made it easier to squeeze a digital film into a computer file; and the increased trading of movies over file-sharing networks, such as LimeWire and Morpheus, and through Internet chat-rooms. It is now possible, as Michael Eisner, Disney's boss, demonstrated at a Senate hearing last month, to capture from the Internet a brand-new film, such as “Monsters Inc”, or a current TV show.

Naturally, Hollywood is in a panic. In 2000, the average film cost the big studios $55m to produce and $27m to promote. And four-fifths of a film's revenue typically comes from sales after the release at the movie theatre: from home video, pay-TV and so on. The industry relies on this controlled-release pattern to ensure that it pockets a slice of revenues at each stage. So the idea that a new film can simply be zapped out on the Internet, with no compensation to the industry that created it, causes consternation. Richard Parsons, the new boss of AOL Time Warner, has described it as “worse than shoplifting”.

The movie industry is now trying to combat this with both legal and commercial means. The greatest concern is protecting copyright. The fear is that, once a studio releases its films online in digital format, it will relinquish all control over their subsequent use and distribution. The industry's response, however, has been an increasingly heavy-handed effort to fight piracy with technology.

This approach will always have limits because no form of encryption is impenetrable. Just look at the $1 billion lawsuit filed last week by Canal Plus, alleging that NDS, a subsidiary of NewsCorp, cracked and distributed on the Internet the codes to the French company's pay-TV encryption system. But the movie industry is behaving with particular severity. It has already tried to ban the sale of digital TV-recording devices that allow users to share movies via an Internet connection. Now it is backing a bill, put forward by Fritz Hollings, a Democratic senator, to require the computer industry to build copy-protection technology into its hard drives. “The content industry cannot solve the piracy issue alone,” argues Peter Chernin, president of NewsCorp.

The other approach is to try to thwart piracy by supplying a legal alternative. This is what the record companies did, by setting up their own subscription download services. Even Napster, now backed by Germany's Bertelsmann, is hoping shortly to relaunch as an official business, its underground version having been closed last year.

Later this year, five big studios—Sony Pictures, Paramount Pictures, Universal Studios, Warner Brothers and MGM—plan to launch movielink.com. Movie fans will be able to download recent and archive films from this site, for a fee. One day, online distribution might even become profitable. “Every time consumers have a new medium for watching movies, this has increased the overall revenue stream,” says Yair Landau, head of Sony Pictures Digital Entertainment.

Because of their concerns about copyright, though, the studios' plans are half-hearted. Movielink.com will, in effect, rent its films. Users will not be allowed to “burn” them on to a DVD, transfer them to another device, such as a television set, or share or swap them in any way. This makes downloaded movies less useful than old-fashioned video cassettes—which undermines the argument for setting up such a service in the first place.

Yet offering a legal download service is a necessary defensive move in the face of relentless technological improvement. Napster thrived because it offered music fans convenience and flexibility that they could not find elsewhere. Filmed entertainment, by contrast, takes up lots of bandwidth and is tediously slow to transfer. At the moment, most people are unlikely to wait several hours to download a pirated film—a trip to the video store is simpler. But better compression technology and faster Internet links will make downloading movies more practical.

When downloading does take off, the trick for the movie studios will be to find a reasonable balance between protecting their revenues and keeping consumers happy. The meaner the industry is over what people can do with the movies they pay to download, the more the studios' own services will be a second-rate alternative to piracy.

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Face value

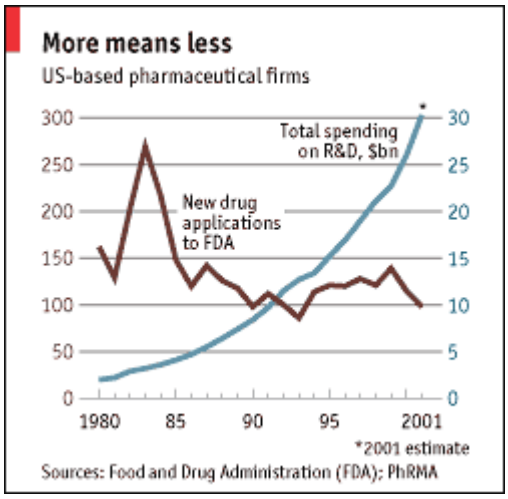
Searching for a new formula

Mar 21st 2002
From The Economist print edition

A Frenchman with plenty of American in him is shaking up GlaxoSmithKline

PHILADELPHIA has long attracted able and ambitious Frenchmen. Jean-Pierre Garnier, chief executive of GlaxoSmithKline (GSK), based in the city, is no Lafayette or de Tocqueville, to be sure. But he needs similar powers of analysis and command to run his business.

Leading any pharmaceutical company these days is a tough task. Whereas investment in research and development (R&D) is on the rise, productivity has levelled off (see chart), and some products for which companies had the highest hopes have failed to pass muster with the drug regulators, or have had side-effects that caused them to be pulled from the market. Meanwhile, patent expiry is hitting firms' sales and share prices; according to Lehman Brothers, new competition from generic rivals this year may affect 13 drugs with combined annual sales of almost $10 billion in America alone.



But GSK is not just any pharmaceutical company. Incorporated in Britain, it is the world's second-biggest maker of drugs, with 100,000 employees producing more than 70 prescription medicines, from anti-malarial to anti-asthma drugs, with sales last year of £17.2 billion ($24.8 billion). Managing such a giant is hard enough, but GSK is a particularly tough case since its scale comes from the merger of two sprawling companies, Glaxo Wellcome and SmithKline Beecham (SB), in 2000. Earlier attempts by the companies to unite foundered on personality clashes between their bosses. As neither wanted to step aside, Mr Garnier, then chief operating officer of SB, was a compromise.

GSK's recent performance has proved the wisdom of this choice. Last month, Mr Garnier announced a 16% rise in annual pre-tax profits, to £6.2 billion, and £1.8 billion in merger-related savings by 2003. This comes as no surprise to those who have watched his 27-year career in the industry. Although his early training in France was in pharmacology, Mr Garnier made his name in marketing, and is credited with much of the success of SB's leading products: Paxil, taken for depression, and Augmentin, an antibiotic.

Such skills will come in handy as GSK tries to find new outlets for its existing product line in order to maintain profitability until new blockbusters emerge. Mr Garnier's interest in marketing runs in the family: his father worked for Havas, a big French advertising group, as a turnaround artist, rescuing troubled operations.

Mr Garnier is a curious combination of continental charm and American efficiency. His easy-going manner and casual dress are a stark contrast to Sir Richard Sykes, the wry and dapper ex-boss of Glaxo Wellcome who will shortly step down as chairman of GSK. Sir Richard is famous for his grand vision of the drug industry's future. Mr Garnier has equally ambitious goals—such as making GSK the most productive company in its sector—but is more of a careful pragmatist.

He is also seen as a hands-on chief executive. This is a cultural change for the survivors of Glaxo Wellcome, which has seen most of its top executives melt away, and many of the new company's

leaders, including Mr Garnier and the head of R&D, settle in the United States. Mr Garnier is at pains to point out that GSK still has strong roots in Britain, where more than two-thirds of its shareholders are based. Yet he clearly sees the company's future in America, where it earns over half of its revenues.

Opening up

Gallic flair notwithstanding, Mr Garnier is not one for elaborate politesse. His curt public dismissals of fellow drug companies have created a stir. But when it comes to big issues, such as how to get costly new drugs to the poor, such straight talking is welcome. GSK has led the way in discount pricing for the poor—in America and Africa alike—and voluntary licensing of its patents. Development agencies are impressed by Mr Garnier's willingness to look at unconventional solutions, such as his personal appeal to Bill Gates to help fund development of GSK's new malaria vaccine.

Such openness to new thinking goes to the heart of the company. Mr Garnier has introduced a radical new structure for GSK's 16,000-researcher-strong R&D effort. The creative bits of drug making have been divided into six centres, each focused on a clinical area, such as metabolic disease. Each centre has its own management team, chooses its own projects and cuts its own deals with biotech firms. Centres that meet their productivity targets will be rewarded with a bigger slice of the R&D budget than their underperforming peers. The best can even expect a share of the royalties.

At the moment, GSK has 42 new chemical compounds in early-stage clinical trials. But the company may not maintain its current growth rate while these drugs slowly make their way to market. Mr Garnier frowns on suggestions that GSK might consider another merger: it already has everything it needs to succeed, he says. The company plans to launch a few interesting medicines this year, some of them licensed in from other firms, but none considered blockbusters. It also faces anxiety over intellectual property: last week, a court rejected GSK's defence of its remaining American patents on Augmentin. GSK plans to appeal.

Mr Garnier is philosophical about such struggles. Since no drug accounts for more than 12% of sales, GSK is insulated from the sudden-death syndrome that afflicts some companies when their blockbuster loses protection. Still, he would like to see the patent system reformed to give patent-holders a fixed term of exclusivity from the time of marketing, rather than from an earlier stage of development when outcomes are less certain.

Ultimately, of course, success in the pharmaceutical industry lies in innovating for the future, not fighting over the past. Mr Garnier frankly admits that GSK's new approach is not guaranteed to deliver. But he is absolutely certain that the old way will no longer do.

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Luxury goods

Every cloud has a satin lining

Mar 21st 2002 | NEW YORK
From The Economist print edition

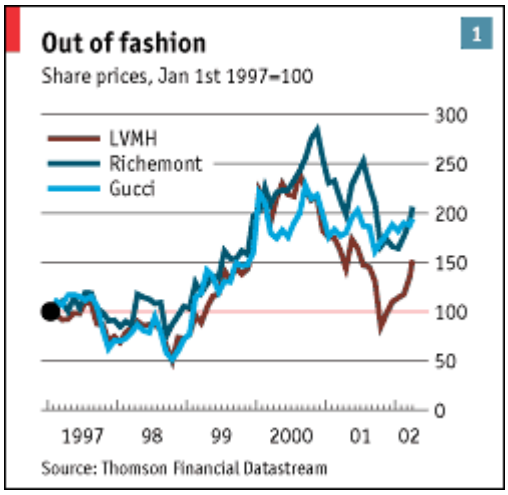
Luxury-goods companies are being remodelled by today's tough economic times—some of them into better shape

CAN this really be the right time to invest in luxury goods? Miuccia Prada obviously thinks so. The granddaughter of the founder of the Italian fashion group has just opened spectacular new stores in quick succession in New York and London. With its magic mirrors, plasma displays and computer-controlled changing rooms, Prada's two-month-old shop in Manhattan cost a staggering $40m, sits just a mile from Ground Zero, and sells practically nothing. The group's Jil Sander store in London opened in February. Located symbolically between Bond Street and Savile Row in a refurbished Georgian mansion, its 10,000 square feet are divided by “floating curvilinear walls” and look as busy as Brighton beach in a blizzard.

The luxury-goods business has been hit in swift succession by a weakening global economy, an enduring slump in Japanese spending, and the September 11th terrorist attacks. The Japanese, who used to buy a third of the world's luxury goods, cut their foreign travel in half after the attacks and tightened their Louis Vuitton purse-strings. At the same time, wealthy Americans stopped flying, which had a dramatic effect on the luxury-goods purveyors of London, Paris and Rome.

At home too, Americans' attitudes to luxury changed, at least temporarily. “Conspicuous abstention” replaced voracious consumerism among the fast-growing, younger breed of newly rich. The decline in job security, the lower bonuses in financial services, and the stockmarket bust that wiped out much of the paper wealth generated in the late 1990s, bred a new frugality. Sales of expensive jewellery, watches and handbags—the products that make the juiciest profits for the big luxury-goods groups—dropped sharply.

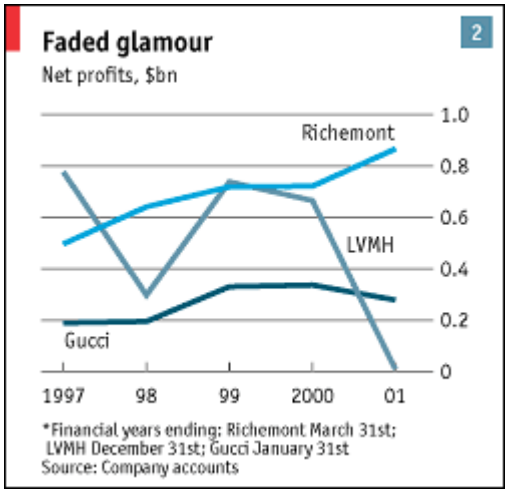
The impact has been most striking among the handful of large, quoted luxury-goods companies (see chart 1). France's Louis Vuitton Moët Hennessy (LVMH), the industry leader, issued four profits warnings after September 11th and ended up reporting a 20% decline in operating profit for 2001, after having repeatedly promised its investors double-digit growth; Richemont, a Swiss company that is number two in the sector and owns such brands as Cartier, Mont Blanc and Piaget, reported a 13% drop in same-store sales for the quarter to the end of December; and Italy's Gucci Group, the third largest, announced this week that second-half profits dropped by 33% (see chart 2). Meanwhile, privately held Prada had to postpone its stockmarket flotation and was forced to sell (to LVMH) a recently acquired stake in Fendi, a prestigious Italian bag maker, in order to reduce its debts.



Democratising luxury

So has Ms Prada completely lost the plot in opening her showy shops in London and New York? Maybe not entirely.

In the first place, the super-rich are still untying their purse strings for the right products. Hermès Birkin handbags, for instance, which sell for up to $13,000 each, have in some places a waiting list extending for years. And certain luxury toys for the boys are still in great demand. Becker Automotive Design, a Los Angeles firm that soups up sports-utility vehicles with cocktail cabinets and satellite computer links at $85,000-250,000 a go, is expecting its business to double this year.



What's more, these consumers are increasing in number all the time. “High net worth individuals” they are usually called by those with an eye on relieving them of some of their worth. Merrill Lynch, an investment bank, and Cap Gemini Ernst & Young, a consultancy, have estimated that there are more than 26m such people in the world—defined as individuals with investible assets of over $1m. By 2005, they estimate that number will have increased by some 50% (see chart 3).

The Geneva motor show this month was full of luxury new vehicles targeted at this tempting market. They included a new Bentley costing $150,000 and DaimlerChrysler's $300,000 Maybach, a model which will come fitted with reclining seats and a humidor. “These cars create their own demand,” said Jürgen Schrempp, the chairman of DaimlerChrysler.

Higher and higher 3

Wealth by region of high-net-worth individuals* $trn

	North America	Europe	Asia	Latin America	Rest of world	Total
1997	5.9	4.8	4.0	2.5	1.9	19.1
1998	6.9	5.6	4.4	2.7	2.0	21.6
1999	8.1	6.7	5.4	3.1	2.2	25.5
2000	8.3	7.2	4.9	3.3	2.8	26.5
2005†	13.0	10.5	7.3	4.8	4.1	39.7

*Those with investible assets of $1m or more †Forecast
Sources: Merrill Lynch; Cap Gemini Ernst & Young

More significantly, though, there is a new type of luxury-goods consumer who promises to expand the market dramatically. Typified by the characters in the TV comedy “Sex and the City”, these consumers are in effect democratising luxury, says Michael Silverstein, a consultant with the Boston Consulting Group who is writing a book on the subject. He defines the phenomenon as: “the selective trading-up of middle-market consumers to higher levels of quality, taste and aspiration”.

Carrie Bradshaw, the star of the style-setting sitcom, is the archetypal new luxury consumer. In one recent episode, she applied for a mortgage from her bank but had to confess that her only collateral was the $700 in her current (checking) account and the $957 in her savings account. Needless to say, her application was turned down. She later admits to her friend Miranda that she has about 100 pairs of shoes costing an average of $400 a pair. “$40,000,” gasps Miranda, “there's your down-payment.”

The new consumers of luxury goods are, as Mr Silverstein puts it, “simultaneously trading up and trading down”. Carrie has enough Manolo Blahnik shoes for several lifetimes, but she cannot afford a decent roof over her head. Upmarket Porsches and Audi Quattros live out on the streets in the most modest suburbs; $10 tops from H&M are worn with $500 bags from Gucci.

These new customers—luxury-rich but asset-poor—are both an opportunity and a threat to the traditional luxury-goods producers. As consumers, they are more demanding, more selective, and show less brand loyalty than the “high net worth individuals” who were the archetypal consumers of the old luxury. They are willing to pay high prices, but they expect commensurate quality; old luxury was never so fussed.

And they want the hottest, trendiest designs, which increasingly have to be marketed in creative (and expensive) ways—including product placements on TV sitcoms. Carrie has done wonders for Manolo Blahnik, while her friend Samantha's episode with a Hermès Birkin handbag only went to lengthen the queues already lining up for the product.

This democratisation of luxury is, however, eating into the profits of the luxury-goods manufacturers. To maintain quality and to withstand the tightening of their margins that it implies, they must have the capacity and resources to change designs frequently and to get new products into the shops rapidly. That means money, discipline and clout.

This is not good news for the smaller family firms that abound in the industry. Antoine Colonna, an analyst with Merrill Lynch, says that “the interests of family shareholders looking to maximise their wealth are not always compatible with the heavy investment needed to generate medium-term profits.”

The age-old industries of designing clothes, crafting jewellery and brewing refined tipples still remain largely under the control of their founding families and designers, either as small private businesses or as part of conglomerates that allow them to operate independently. Mr Colonna estimates that the three big publicly-quoted companies control just a quarter of the global market. Further concentration is overdue.

The car industry has been consolidating its luxury (and often family-based) brands for some time. Many of the grandest names on the road have been gobbled up by the big mass-market producers. Bentley, Lamborghini and Bugatti are all owned by Volkswagen; Aston Martin (the original James Bond car) is owned by Ford, and Ferrari by Fiat. BMW, meanwhile, takes over perhaps the grandest of them all, the regularly loss-making Rolls-Royce, from the beginning of next year.

This process of consolidation has begun to take place in other areas of luxury, and the recession has given it an extra push. Over the past few years LVMH has added many famous names to its stable, including Tag Heuer watches, Thomas Pink shirts, and Phillips, a London auction house. Gucci has bought Yves Saint Laurent, Balenciaga and Boucheron. Not all of these have been unmitigated successes. LVMH sold its majority stake in Phillips earlier this year after making such a mess of it that it lost the group an estimated *euro*110m ($98.4m) last year.

Prada bought Helmut Lang, Church's shoes and Jil Sander, although Jil Sander herself left soon after Prada bought the label in August 1999. Like many others, she found herself unable to work with Miuccia Prada's husband, Patrizio Bertelli, who runs the business. It is an industry prone to such flouncing. Domenico De Sole, the chief executive of Gucci Group, admits (though he exempts his own firm) that “the luxury-goods business is particularly susceptible to a lack of discipline”. Donatella Versace, who has been the public face of the family firm since her brother Gianni was murdered in Miami in 1997, uses the company plane to fly her daughter to school.

Design and creativity are the bedrock of any luxury brand. But the access to financial resources and thorough execution that are part of any professional management really come into their own when times are tough. The vulnerability of small trophy companies becomes more obvious during a downturn.

“People think about the luxury business in the wrong way—they think about brands. But luxury companies are primarily retailers”

Execution, execution, execution

Luxury is an unusual business. A luxury brand cannot be extended indefinitely: if it becomes too common, it is devalued, as Pierre Cardin and Ralph Lauren proved by sticking their labels on everything from T-shirts to paint. Equally, a brand name can be undermined if it is not advertised consistently, or if it is displayed and sold poorly. Sagra Maceira de Rosen, a luxury-goods analyst at J.P. Morgan, argues that, “If there is one critical word in the luxury business, it is ‘execution’. People think about the luxury business in the wrong way—they think about brands. But luxury companies are primarily retailers. In retailing, the most important thing is execution, and execution is all about management. You may have the best designed product, but if you don't get it into the right kind of shop at the right time, you will fail.”

She cites the example of Fendi, whose handbags and clothes are beautifully made but often in the shops at the wrong time. Gucci and Yves Saint Laurent suffered from similar lapses in the early 1990s. Poor control of distribution and display, poor control of the product quality and price, and an over-extension of their brands nearly crippled both businesses.

That explains why Gucci has spent so much time and effort buying back control of its licensees—both the Gucci label and, more recently, the group's newly acquired Yves Saint Laurent (YSL) label—and opening chains of directly owned and operated stores for both brands. Today, 80% of Gucci's and Hermès's products, and 100% of Louis Vuitton's (considered one of the greatest luxury brands) are sold through directly owned and operated stores. To be able to do that requires not just high-calibre management, but the kind of money that only the capital markets can reliably supply.

The type of business that can attract the necessary management talent and financial firepower to put such a strategy into effect is, almost by definition, a quoted company that can raise money on the

stockmarket and issue stock options. It must also be large enough to harbour several brands, and so not be tempted to over-exploit (and so destroy) a single label. That means having a pipeline of brands and products “under development”, and devoting considerable resources to old-fashioned “R&D”.

The new chemistry

The model for the luxury-goods companies of the future is not the sprawling, multibranded conglomerate—typified by LVMH with its mix of unrelated luxuries, including clothes, wine, cosmetics, champagne and, until recently, auction houses. Nor is it the retailer selling other people's brands or its own single brand. Rather, it more closely resembles big pharmaceutical groups which combine the management of a pipeline of brands at different stages of development, heavy investment in the creation of new products, and effective marketing and distribution.

Currently there are few professional luxury-goods companies with sophisticated brand pipelines, since so many labels are still individually owned and run. Even among the quoted conglomerates, Louis Vuitton still makes up the bulk of LVMH's non-spirits sales, and the Gucci brand accounts for 80% of Gucci.

“Today, in the luxury sector, you have very few star brands,” says Bernard Arnault, the boss of LVMH. And you can't conjure them up overnight. “You need at least 30 years”, he claims, “to build such a brand. But when you have got some, you can resist any crisis.”

Although it is the market leader today, LVMH has faced questions about its management quality ever since Mr Arnault blew $1 billion on various Internet ventures (largely through his own private firms) and bought the burdensome Phillips auction house—not least because his main French rival, François Pinault, had previously purchased Christie's, a much larger auctioneer. Before he finally sold Phillips in February this year, Mr Arnault admitted that there were no synergies between auctioneering and all his other businesses.

Nor has LVMH's foray into retailing (through the DFS duty-free stores and the Sephora perfume chain) been a great success. According to Olivier de Combarieu of Fitch, a credit-rating agency, “DFS and Sephora are a complete nonsense as part of LVMH. LVMH has confused the retailing of luxury with retailing others' brands—a low margin business that it should not be in.” Mr Arnault has said that he will not sell off the two units until he has made them profitable.

LVMH has not been particularly good at nurturing brands either. After years of investment, its Celine and Loewe brands are still “irrelevant”, says Ms de Rosen. Richemont, under its chief executive, Johann Rupert, has done a much better job, constructing a portfolio of successful watch brands, with Cartier at the core but also now including Piaget and Mont Blanc.

But the company to watch is Gucci. It is focused, careful and disciplined. Mr De Sole admits that his leading brand, Gucci, will run out of growth eventually. But, like a drug company with its pipeline, he has been developing replacements, from the restructured YSL to the revitalising of veteran brands such as Balenciaga. And he has gone on investing throughout the recession, especially in YSL where the group will spend $200m this year expanding its stores and ready-to-wear collection. It is not expected to make a profit until 2004.

But the company to watch is Gucci. It is focused, careful and disciplined

As with other industries, technology is increasingly important (and expensive) for the luxury-goods business. For example, the scribbles of Tom Ford, Gucci's star designer, are fed into a sophisticated computer system where they can be seen in three dimensions and in different colours to help the designer spot flaws or tweak shapes before a prototype is made. Gucci has also invested in computer-aided water-jet cutters that shape the leather for its handbags and other accessories. The same machine can also choose the quality of leather to cut for the requirements of, say, the inside or the outside of a bag.

The prize for finding a blockbuster luxury product is much the same as in the pharmaceuticals industry: magical margins. Losec, Astra Zeneca's best-selling ulcer drug and an alternative to GlaxoSmithKline's Zantac, has gross margins of around 85% and operating margins of more than 25%. Gross margins on Louis Vuitton, Gucci and Cartier are all around the 70% mark; their operating margins are over 20%. Sumptuous business if you can get it.

For these big firms' smaller rivals, the current downturn merely throws into sharper relief their inability to keep pace. As Mr Colonna of Merrill Lynch puts it, “The family-owned companies are realising the limits of going it alone against these mammoth groups. They just don't have the resources to invest in real estate, distribution and advertising.” As in so many industries, the recession will benefit the strong and accelerate the rush of private companies into the arms of bigger, more professional groups. For the best of them, the future is as bright as a Cartier gem.

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Russia's central bank

Mr Rouble quits

Mar 21st 2002 | MOSCOW
From The Economist print edition

Kommersant

Viktor Gerashchenko's replacement must surely be an improvement on "the worst central banker in history"

Get article background

THE single biggest obstacle to the development of a proper banking system in Russia was probably Viktor Gerashchenko, a wily Soviet-era relic whose second term as head of the central bank ended abruptly on March 16th. His first stint there, in the early 1990s, was marked by financial illiteracy and inflation. Jeffrey Sachs, an American economist, dubbed him "the worst central banker in history". Now, this dinosaur's departure marks an important step on the slow evolutionary path of Russia's financial system.

In past years the central bank has become a byword for pedantic but ineffective regulation, burdening the law-abiding with pointless paperwork and turning a blind eye to the atrocious behaviour of the well-connected. Its other activities have been equally startling. It runs a web of foreign subsidiaries whose purpose is often murky. One of these, based in Jersey, was an energetic speculator in Russian government debt, until Russia's financial crash of 1998. The debt market was run, conveniently, by the bank itself. The bank lied to the International Monetary Fund about the size of its reserves, earning a rare public wigging. Not all of this happened on Mr Gerashchenko's watch, but he showed no enthusiasm for transparency before or since. One of the biggest financial mysteries in Russia is the size and nature of the bank's precious-metals stockpile.

Internal housekeeping is just as idiosyncratic. The bank employs 80,000 people, highly paid and mostly underworked. America's Federal Reserve system, by contrast, has about 23,000 (albeit for a narrower range of tasks). Unlike its foreign counterparts, Russia's central bank runs businesses, including a large property empire. There is a big pension fund, managed on misty but generous principles.

Taking over all this is a junior finance minister called Sergei Ignatiev. The main claim to fame of this reassuringly colourless figure is that he is widely regarded as honest—a rare distinction among Russia's elite. Mr Ignatiev's shabby suits, old-fashioned glasses, and austere tastes have left a lasting impression on outsiders who have dealt with him. Yevgenia Albats, an investigative journalist now living in America, recalls: "He is a very, very honest guy. I kept asking why he didn't take bribes. His answer was: 'I just cannot. I will feel bad."

Mr Ignatiev faces three main tasks. The easiest, for the time being, is macroeconomic. Mr Gerashchenko's main success was to keep the rouble stable against the dollar, in nominal terms (see chart). That stability was probably the single biggest benefit of the

past three years. High oil prices and a big devaluation in 1998 have generated a huge trade surplus. This is falling slowly as the underlying uncompetitiveness of Russian industry re-emerges, but it is not an immediate problem for the central bank. Inflation is declining. A more active monetary policy, focusing on interest rates rather than on bullying the currency markets, would be a step forward.

The second task is to manage the bank better. Mr Ignatiev's job will be to replace the bank's crude clout, and reputation for greed, with a new respect for it as an independent institution. That will mean working with the government on reform, while retaining independence on day-to-day decisions. No state institution in Russia has so far managed that.

Trickiest of all is reforming the banking system. The lack of financial intermediation is probably Russia's single biggest economic weakness. Russian banks tend to be small, badly run, and do little deposit-taking and lending. Many are no more than treasury departments for large companies, for channelling money offshore. Some are heavily involved in organised crime. Most Russians keep their savings in hard cash.

Lifting exchange controls would be a tonic for the bank and the economy too: they fail to prevent capital flight of over$10 billion a year and are rich soil for corruption. Mr Ignatiev says he wants them removed, but slowly.

Sorting all this out will be difficult. Bad banks must be closed: that means taking on some of the nastiest people in Russia. Confronting powerful criminals is possible these days, at least if you have Kremlin backing. It is already under way in the energy industry, where some notorious figures are facing jail terms. But it will be nerve-wracking and time-consuming.

At the same time, honest banks need more flexible and sensible rules. Making electronically stored data legally acceptable would be a start; so would simply changing the rules on how cash is handled in a bank branch.

The biggest challenge of all is Sberbank, the state-owned behemoth that holds the majority of the country's savings. Its size and de facto state guarantee heavily distort the market. Some reform has started in the past year or so. Regional political bosses are no longer allowed to use its branches as their personal piggy-bank. But at some point it will need to be split up.

So far Mr Ignatiev has sounded cautious. However well he fills the new job, the central bank alone cannot change things much. A proper financial system sits on an intricate foundation of established institutions and habits—functioning courts, for example, or credible accounting—almost all of which Russia still lacks. The changes in banking, as in other things, will not be sweeping or speedy. But at least the central bank should no longer actively hinder them. That is a welcome change.

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Accounting

Picking over Andersen

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Rivals and lawyers swarm around the wounded accounting firm

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LIFE at the bean-counting firm of Andersen these days is definitely not boring—predictions of its ultimate fate change by the hour. In recent days, Andersen's operations in Russia, Spain, Chile and Asia were all said to be wrangling over separate exit strategies—on March 21st, partners of Andersen Hong Kong and China agreed to combine their practices with PricewaterhouseCoopers. There was still hope of a broad agreement for Andersen's non-American operations to join KPMG. Again, no one is ruling out a deal with PwC, Ernst & Young, or Deloitte Touche Tohmatsu, the remaining members of what were once known as the Big Eight—now commonly referred to as the Final Four.

Equally possible is no deal at all. Indeed, the negotiations with KPMG appear more like playing for time than a prelude to a transaction. Under the current framework, due diligence by each firm would begin on April 1st and continue for two or three months; negotiations, as well as efforts at global regulatory approval, would approach a conclusion not before October at the earliest—a lifetime away for a haemorrhaging firm. Giant obstacles loom, notably the competition commission in Brussels, which prides itself on its global reach. In the meantime, Andersen faces a barrage of litigation.

On March 20th Andersen pleaded not guilty in a federal court to charges of obstruction of justice stemming from the destruction of documents tied to Enron's rancid financial statements. Jury selection will begin on May 6th. While criminal prosecutions have proved deadly for many American financial firms, the heavier sword hanging over Andersen's head is shareholder suits. Complaints must be filed by April 1st. The case, barring a settlement, will run for years. Andersen's liability for its ties to Enron could be as large as any assets mustered by the firm—and those of any potential acquirer, thus blocking an American suitor. Lawyers for plaintiffs in America intend to push this further to include foreign branches as well.

Their efforts will begin with Enron's British operations, since destruction of Enron's documents occurred not only in Houston but also in London. Then, they will argue that Andersen Worldwide, the partnership's formal name, is an international corporation, not, as Andersen will argue, a series of distinct operations in 83 countries outside America. Tying in all of Andersen's operations offers prospects of a greater recovery, since the non-American side produces more than half of Andersen's revenue and income. It also raises the possibility of a stronger firm, to be milked by litigation for years. Without affiliates outside America, Andersen might be unable to audit large, international firms.

Already, a plaintiff lawyer says, work is proceeding on litigation against Andersen because of questionable revenue figures reported by Global Crossing, a bankrupt telecom firm that was its client. Auditing firms that acquire Andersen clients will try to immunise themselves from litigation by vetting these companies with particular care: that could produce more suits against Andersen. Faced with mounting claims, a last resort may be to create a second company similar to Equitas, which was set up by Lloyd's of London, with court approval, to deal with insurance claims.

Inside Andersen, life is becoming more difficult. Senior partners are immersed in meetings to save the firm, as well as attempts to mollify clients and key employees who are heading for the door. Thousands of people are expected to find themselves redundant following the loss of 41 large auditing clients.

“I would like to be optimistic about Andersen but in the end it comes down to whether they want to survive or not,” says Paul Volcker, a former head of the Federal Reserve who was brought in by a harried Andersen as chairman of an oversight board. “I believe they could if they find the energy and the will to do so.”

Can they? So far, the most focused response has come from Andersen's big competitors. Of the 11 lost clients with more than $1 billion in annual revenue, four have gone to Ernst & Young, three to PwC, and two to Deloitte Touche, according to Auditor-Trak, a service of Atlanta-based Strafford Publications.

If there is a silver lining, it is a sense that Andersen's travails may be having a positive impact on the profession. Demands for thorough audits are growing, and firms winning business from Andersen will need help. Meanwhile, the pool of accountants is relatively fixed and it can take six years of training in many states to produce new ones, says Jonathan Hamilton, managing editor of *Public Accounting Report*.

What had been a buyer's market has now turned. At the high end, Peter McLean, head of the financial officer practice at Spencer Stuart, a corporate recruiter, says that using certified public accountants (CPAs) as chief financial officers had been on the wane in recent years: companies favoured people versed in mergers and the Wall Street culture. Now there is a renewed emphasis on control and risk management, once the hallmark of the well-trained CPA.

The demise of Andersen would bring to a fast conclusion Mr Volcker's oversight board. It had quickly developed an extensive agenda for reform, addressing failings that critics have raised for years, such as endemic conflicts of interest within accounting firms. In recent discussions, the board has decided to continue opining on industry reform even if it loses its formal authority. Given the problems revealed by recent accounting scandals, there is a desperate need for a credible group to emerge with a plan. The federal government has waffled about the issue for years, while the industry has fallen short on efforts to regulate itself. Andersen, in its effort to become credible, may yet have made a contribution to a better industry.

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Accountancy in China

Enronitis delights local auditors

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Big-five audits are no longer the standard to aspire to

Get article background

LOCAL accounting firms in China are chortling at the woes of Andersen, Enron's auditor. Last December the China Securities Regulatory Commission (CSRC) issued a new rule that companies wanting to issue new shares must pay for an additional audit by an international firm in accordance with international accounting standards. Local firms, fearing a massive loss of market share to foreign rivals, attacked the rule. Now the CSRC has modified it, largely because, in the light of Andersen's part in the downfall of Enron, the commission can no longer insist on the superiority of foreign firms.

The CSRC pushed hard for western standards as a response to a string of scandals in which listed Chinese companies issued grossly inaccurate financial reports not corrected by their local auditors. The most notorious case concerned a biochemical firm, Yinguangxia, which reported a net profit of 417m yuan ($50m) in 2000 but which, according to CSRC investigators, had actually lost 150m yuan. The firm's accountant, Zhongtianqin, was one of China's largest and most reputable: its licence has since been suspended.

This scandal, and several like it, seemed to indicate that the CSRC had the right idea, and that the sooner China learned western standards the better. But Andersen's failure to stop Enron inflating its results suggests that China's firms are not so bad by comparison. This month the CSRC said that additional auditing would be necessary only for companies issuing 300m or more shares.

The retreat will please the Ministry of Finance, which wants Chinese standards and practices to move closer to international ones without adopting them outright. China's unique characteristics, it believes, require a unique regulatory system. The ministry has close ties to the domestic accounting industry, which would lose out if foreign standards (and firms) won preference.

According to Professor Chen Xiaoyue, vice president of the National Accounting Institute in Beijing, Andersen's entanglement in the Enron meltdown has changed the debate over standards. But he also insists that China's real problems have less to do with standards than with bigger issues of law and regulation.

According to Mr Chen, Chinese courts are ill equipped to handle complex cases involving large numbers of plaintiffs and allegations of exotic accounting. Another factor is the structure of China's capital markets. With price-to-earnings ratios running as high as 50 and 60 for Chinese firms, any exaggeration of earnings can translate into huge share-price gains.

Professor Chen Zhiwu of the Yale School of Management says there are so many people profiting from such puffery that there is little demand for accurate financial reporting. Chinese investors expect the government to step in to reverse any sharp decline, either in individual stocks or in the overall market, and so there is little reason to link a company's performance to fundamental figures. The debate in China, he says, should focus less on the role of the CSRC and more on the courts, the media and market participants themselves.

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Airline insurance

Terror in the air

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Governments are under pressure to remain insurers of last resort

AP

Uninsurable impact?

TO BUOY the competitiveness of European airlines, EU governments are expected to renew their guarantees next week as insurers of last resort for terrorist attacks on aircraft. They will be following the American government, which has extended its guarantee for airlines based in America until mid-May. Both American and European guarantees had been due to expire on March 31st.

A serious event can fundamentally change a risk's insurability. The chances of a terrorist act in the air used to be considered so remote that aviation insurers wrote insurance for third-party liabilities from acts of terrorism and war for no additional charge. The cover for damage done to people and property on the ground was part of airlines' "all risk" insurance, which also covered the aircraft and its passengers. This changed after the terrorist attacks last September that caused billions of dollars of damage to third parties. Cover for third-party terror risk became the hardest to get and the most expensive of all insurance policies for airlines. Few insurers are now prepared to insure it, or only at sky-high rates and for cover that airlines consider insufficient.

So now third-party terror risk is a huge headache for airlines. Insurers withdrew cover for it immediately after the attacks of September 11th. They reinstated it only hesitantly a couple of weeks later, after cutting it to a maximum of $50m per aircraft, per event. To avoid entire fleets being grounded—airlines threatened not to fly without sufficient insurance—the American and EU governments stepped in to back airlines' war and terrorist risk for a limited period.

The American government has already agreed two weeks ago to continue its backing. It is also supporting Equitime, a captive insurer that is being set up in Vermont by Marsh, an insurer, the Air Transport Association, a trade group in Washington, and the federal government's Department of Transportation. (Captives are insurance or re-insurance vehicles set up by one or more companies to insure the parent companies' risk.)

Equitime was favoured over a proposal by a consortium led by American International Group (AIG), a giant insurer. Open to every American airline, the captive will provide cover for up to $1.5 billion for passenger and third-party war and terror risk. Equitime will initially be capitalised at about $300m, but it will progressively fill its coffers with airlines' premiums. The federal government remains insurer of last resort. The AIG consortium on the other hand offers to supplement the $50m available in the primary aviation market to cover third-party terror risk up to $1 billion.

Airlines prefer Equitime: it will be less expensive than the AIG consortium's policy, which requires a surcharge of around $3 on each air ticket. And it offers better cover, since the government has deep pockets.

Insurers and airlines differ on what is adequate insurance against terror. Unsurprisingly, Hank Greenberg, the chairman of AIG, says there is already enough insurance available in the private sector. There is no need for a permanent government role, insists Robert Hartwig at the Insurance Information Institute in New York. But if, heaven forbid, another September 11th happened, says Michael Frinquelli at Renaissance Fund Advisors—a hedge fund that invests in insurance companies—the AIG cover won't be enough.

Europeans are having a similar debate, with some time-lag. EU governments waited for the American decision before determining their next step. Next week Europeantransport ministers are meeting in Brussels to debate airline insurance.

“Americans do it right and we copy them,” says Karl-Heinz Neumeister at the Association of European Airlines (AEA) in Brussels. Allianz, a German insurer, is putting final touches to the European equivalent of the AIG policy. It will offer airlines cover for third-party terror risk of up to $5 billion for five unrelated events. The price is likely to be lower than that of the AIG policy, but it will require governments to be insurer of last resort.

Permanent government involvement in insuring certain types of terrorist risk already exists in Spain, Britain, Israel and South Africa. Terrorist outrages in these countries caused insurers to run away from insuring such items as exposed commercial property, and governments willy-nilly took on these “uninsurable” risks. For instance Britain's Pool Re, a mutual re-insurance pool with the government as a back-stop, was set up after a series of bombings on mainland Britain by the Irish Republican Army: it insures property against terrorist attacks by bombing or fire. Even though Pool Re has worked well, the British government is noisily reluctant to continue to back airlines' terror risk. It may have little choice, at least until a European or even a global Equitime-type scheme is set up.

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Allfirst's foreign-exchange losses

Crying wolf

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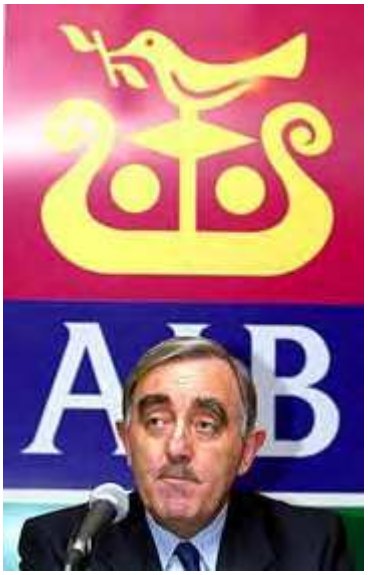
The luck of the Irish



Buckley in the lupine soup

IN HIS rampage through the foreign-exchange market, John Rusnak piled up losses of $691m at Allfirst, the American subsidiary of Allied Irish Banks (AIB). He may have been a “lone wolf”, but he had plenty of witting or unwitting allies.

Six of them were fired from Allfirst last week, after the release of a report by Eugene Ludwig, a former comptroller of the currency. Frank Bramble, the chairman of Allfirst, also announced a previously planned retirement. Two others, foreign-exchange salesmen at Citibank who had dealt with Mr Rusnak, were fired on March 18th, although they were thought only to have excessively “wined and dined” the lone wolf.

Will more heads roll? Cries for the scalp of Susan Keating, chief executive of Allfirst, and even of Michael Buckley, chief executive of AIB, have gone unheeded. How much are the top folk ultimately responsible for the comedy of errors at Allfirst unveiled by Mr Ludwig? The memory of Mr Bramble seems to have failed him at crucial points when others say they gave him warnings about Mr Rusnak's trading. Certainly Mr Ludwig's report recommends that, in future, the chairmen and chief executives of AIB and any operating units should “affirmatively take full responsibility for the trading activities of the bank”.

The report paints a picture of poor structure and mismanagement at Allfirst, which created ideal conditions for the not-so-“lone wolf” to operate in. Mr Rusnak was hired in 1993 as a speculative foreign-exchange trader. In 1994 he had already breached his trading limits, but indulgent controllers shrugged this off as “trader error”. His immediate supervisor, Robert Ray, knew about bonds but not foreign exchange. His immediate controllers lacked experience and Mr Rusnak and Mr Ray were able to bully them out of questioning the star trader's behaviour. The Allfirst treasurer, David Cronin, was too conciliatory: when rows blew up he simply asked colleagues to “treat each other respectfully”.

Mr Rusnak was able to hide increasing losses from foreign-exchange speculation by constructing bogus option trades that apparently offset those that were genuine. Since they required no net transfer of cash, he successfully argued that they did not need to be confirmed by the back office.

A running tab with two big trading counterparties, Citibank and Bank of America, allowed Mr Rusnak to trade without necessarily having to report each trade internally. What's more, the prices at which he traded were not checked independently. Until April 2001 he could, and did, manipulate the market prices fed from Reuters, since they came into Allfirst through his computer. Mr Rusnak was able to trade at will, after office hours, from home, even on vacation. His trading conversations were not recorded. These were all serious risk-management bloopers.

Both Citibank and Bank of America cross-checked with AIB in Dublin about some large trades initiated by Mr Rusnak, but they were given the green light. The lone wolf was finally hunted down on January 30th this year, when Allfirst controllers called banks in Asia to discover that trades which Mr Rusnak claimed to have done with them did not exist.

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Foreign aid

A feast of giving

Mar 21st 2002 | WASHINGTON, DC
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Europe and America are suddenly competing to be generous

EPA

Bono and Bush—aid brothers

THIS has been an extraordinary few days for the world's poorest countries. As hundreds of government officials and aid activists gathered in Monterrey, Mexico, for a big United Nations conference on financing development, several of the world's richest countries have pledged big increases in their aid budgets.

George Bush sprang the first surprise. On March 14th, he announced that the United States would spend an extra $5 billion on foreign aid between 2004 and 2006. With Bono, the rock-star-turned-development-lobbyist, at his side, Mr Bush made a speech that might have been written by the foreign-aid fraternity. The evidence showed, he said, that aid worked where countries adopted sound policies. So the extra American funds would go into a new “Millennium Challenge Account”, exclusively for countries with good governance, investing in health and education and encouraging economic freedom.

Mr Bush's words stunned the aid lobby. Though the amounts were not large—administration officials last week suggested that the proposed $5 billion implied increases of roughly 15% to America's $10 billion budget for development aid—the rhetoric was new. Nancy Birdsall, head of the Centre for Global Development, a new Washington think-tank, called Mr Bush's speech a “philosophical breakthrough”. The Europeans were furious, since Mr Bush's proposals overshadowed their more generous announcement on the same day. EU ministers had agreed to raise Europe's spending on foreign aid to an average of 0.39% of GNP, up from the average of 0.33%—amounting to $25.4 billion—that EU members contributed in 2000.

To achieve that target, those European countries which give the least aid in relation to GNP will have to reach at least 0.33% by 2006. With tough budget problems, Germany had long fought such an increase. Now the need for European solidarity and the desire to show up American stinginess prompted it to give in. Assuming Europe's economies grew by 1.5% a year, the EU pledge would mean an extra $7 billion a year in aid by 2006. That seemed rather more than America's pledge of $5 billion over three years.

But then on March 19th the White House “clarified” the American position. Mr Bush's plan, claimed administration officials, was not a total of $5 billion extra over three years, but a gradual “ramp up” of spending so that, after three years, annual American development assistance would be $5 billion higher. In other words, America was proposing a 50% increase of its $10 billion aid budget, not the 15% many had supposed.

Promises for American aid spending in 2006 are easy to make. But, however slippery the financial pledges turn out to be, the rhetoric will be hard to retract. America is now committed to supporting more foreign aid for poor countries with good policies. That alone made the UN gabfest worthwhile.

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Italy's offshore wealth

A double-edged shield

Mar 21st 2002 | ROME
From The Economist print edition

A new law tempts Italians to repatriate offshore money

ONLY 30 years ago, Italy's *spalloni*, or hired bagmen, did a flourishing trade in humping suitcases stuffed with Italian lire across the border into Switzerland. Italian newspapers even carried the rates of exchange for lire banknotes in the Swiss border town of Chiasso.

As Italians grew sophisticated, so did their methods of dodging taxes and exchange controls. Buoyant foreign trade helped to build up funds beyond the authorities' reach: under-invoiced exports and over-invoiced imports created differences that ended up in offshore accounts. One estimate puts the total of undeclared offshore assets owned by Italians at some *euro*500 billion ($440 billion). No wonder the government wants to lure this home.

Under a law called the *scudo fiscale* (tax shield—because assets return anonymously through trust companies), Italians have a deadline—initially February 28th, now extended to mid-May—to repatriate offshore wealth. The law allows them to set their affairs straight for a modest penalty of 2.5% of the value of the returning assets. However, the assets then become liable for onshore Italian taxes.

There are several reasons why law-breaking Italians should seize this moment to get legal, says Domenico Siniscalco, director-general of the Treasury. The financial-risk factors, which endangered Italians' savings until around ten years ago, have vanished: the lira and many neighbouring currencies have disappeared into the euro, so devaluation is less likely to hurt savings. The European Central Bank keeps the lid on inflation. Default on Italy's public debt is near-unthinkable. In addition, reductions in Italian taxes—inheritance tax is being abolished—reduce the fiscal advantage of holding assets offshore.

The *scudo fiscale* offers juicy new business to Italy's banks, particularly those in wealthy northern Italy, where exporters have thrived since the 1960s. Targeting those who have illicit offshore assets, the big institutions and some financial boutiques now brag about their private-banking services. Paolo Basilico, head of Kairos, Italy's first hedge fund, expects that high-yielding alternative investments will be attractive to repatriated funds.

Not all these funds will go into financial investments, however. Marco Silvano is head of private banking at Intesa BCI, Italy's biggest bank, which is well-rooted in the north. He expects it to handle around one-tenth of the funds that return. He thinks that probably half will go into investment in factory plant or into developing business in other ways. There should also be a boost to consumption, especially by those who have inherited offshore wealth and can now enjoy it at home.

Switzerland stands to lose most, since it has probably over half the Italian funds stashed offshore. Small Swiss private banks are expected to suffer, but the damage to big institutions, such as UBS and Credit Suisse, which have developed private-banking and asset-management operations in Italy itself, should be limited. Vittorio Volpi, head of private banking at UBS says the *scudo fiscale* will “wake up Swiss banks to the need for cost-competitiveness, and force Italian banks to learn what real private banking is”.

Probably around a tenth of the funds held offshore will return. No great shakes, but it would give a *euro*50 billion boost to the Italian economy. Moreover, other funds are probably returning undeclared. The *scudo fiscale* suits only the genuinely wealthy, says a senior banker. The less well-heeled will be bringing back their dosh in suitcases.

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Economics focus

No place like home

Mar 21st 2002
From The Economist print edition

Why voting patterns at the Fed might have implications for the European Central Bank

IS THE Fed biased? Even asking the question is enough to ruffle feathers at that august institution. Yet new research suggests that the voting behaviour of the Fed's key policymakers may be surprisingly biased—and, more importantly, in a way that has implications for the European Central Bank.

The Fed's founders were anxious to eliminate the possibility of bias, either in favour of one region against another, or of large banks against small. Indeed, fear of bias had scuppered two earlier attempts to create an American central bank. The complex voting system of the Fed's main policy body, the Federal Open Market Committee (FOMC), is intended to ensure the broadest range of views.

Research into possible bias has tended to concentrate on the voting behaviour of the 12 Federal Reserve Bank presidents, who represent each of the Fed's districts. Only five have voting rights: the president of the New York Fed, and four others on a rotating basis. The votes of this group show the influence of regional, as well as national economic developments. As a guard against this, the seven members of the Washington-based Board of Governors, who have permanent voting rights, outnumber them.

But might the governors also be biased? Ellen Meade, of the Centre for Economic Performance at the London School of Economics, and Nathan Sheets, who is, as Ms Meade used to be, a Fed economist in Washington, examined the voting records of all FOMC members, governors included, between 1978 and 2000*. As a proxy for regional economic trends, they used unemployment rates, calculated for each Fed district (one of the Fed's obligations is to maximise employment); and they focused on dissents from FOMC majority votes.

It turns out that governors tend to vote against the majority when there is a significant gap between the unemployment rate in their “home” region and the national rate. When the regional rate was, on average, 0.7% higher than the national, a governor would vote against the majority view and in favour of easier monetary policy; when it was, on average, 1.1% lower than the national rate, he or she would vote in favour of tighter policy.

Previous research has shown that the board members are generally less hawkish than the district bank presidents. The analysis by Ms Meade and Mr Sheets confirms that board members appear more likely than the bank presidents to dissent in favour of easier policy, and less likely to press for tighter policy against the majority view. It also shows that this is because overall the governors are more sensitive to regional developments than are the district bank presidents.

Meanwhile in Europe

Is this regional bias among FOMC members something found in other central banks? What about the supra-national European Central Bank (ECB), whose structure bears a superficial resemblance to the Fed's? Hard facts are difficult to come by because of the European bank's secretive working methods: it does not publish records of meetings.

The ECB's Governing Council, like the FOMC, comprises two groups: six policymakers based in Frankfurt, plus the heads of the 12 national central banks in the euro area. But at the ECB voting does not rotate—all 18 members have an equal say. That immediately builds in the possibility of national bias, since six countries—currently Finland, France, Germany, Italy, the Netherlands and Spain—have two

representatives on the governing council.

Ms Meade and Mr Sheets were not deterred by the absence of voting records. They devised an experiment to test whether ECB policy decisions might be affected by national loyalties. Since (unlike the Fed) inflation is the ECB's sole policy objective, they made a working assumption that each council member would cast his vote according to the difference between national and euro-area inflation rates, and that he would vote in a certain way if that difference were above a certain threshold. With one exception, it seems that all the interest rate changes made since the ECB started in 1999 were those which would have resulted if all council members had voted simply on the basis of differences in their national and euro-area inflation rates.

There has long been a suspicion that policymakers—not just in the ECB but in a variety of European institutions—retain at least some loyalty to their home country. That, after all, must be one reason why member governments expend so much effort and political capital in trying to secure posts for their own nationals.

So should the ECB try to reduce the scope for national bias in its policymaking? Reform of the ECB's structure seems inevitable if only because enlargement of the European Union, and of the euro area, threatens to make the existing structure unwieldy. A reduction in the size of the governing council, or at least in the number of members entitled to vote, seems likely at some point. The Nice treaty, agreed in 2000, provides for reforms to be proposed.

A reform being proposed by some academics (and considered in some parts of the European Commission) would tilt the ECB towards the Fed, and go even further, by restricting voting to the permanent, Frankfurt-based council members. Given what Ms Meade's and Mr Sheets's findings appear to show, that might not be a reform in the right direction.

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* “Regional Influences on US Monetary Policy: Some Implications for Europe”, by Ellen Meade and Nathan Sheets. Discussion Paper Number 523. Centre for Economic Performance.

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Marjorie Deane internship

Mar 21st 2002
From The Economist print edition

Applications are invited for the 2002 Marjorie Deane internship. This award, financed by the Marjorie Deane Foundation, is designed to provide work experience for a would-be or junior journalist under 28, who will spend three months of the summer at *The Economist,* writing about finance. Applicants should send a letter introducing themselves, with an original article of about 1,000 words intended for the Finance and economics section. Applications must reach us by April 5th, and should be posted to: The business affairs editor (Deane internship), The Economist, 25 St James's Street, London SW1A 1HG

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Human behaviour

Deviations from the mean

Mar 21st 2002
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AP

Biologists are helping economists to explain why humans are not always selfish

AT SOME point during their education, biology students are told about a conversation in a pub that took place over 50 years ago. J.B.S. Haldane, a British geneticist, was asked whether he would lay down his life for his country. After doing a quick calculation on the back of a napkin, he said he would do so for two brothers or eight cousins. In other words, he would die to protect the equivalent of his genetic contribution to the next generation.

The theory of kin selection—the idea that animals can pass on their genes by helping their close relatives—is biology's explanation for seemingly altruistic acts. An individual carrying genes that promote altruism might be expected to die younger than one with “selfish” genes, and thus to have a reduced contribution to the next generation's genetic pool. But if the same individual acts altruistically to protect its relatives, genes for altruistic behaviour might nevertheless propagate.

Acts of apparent altruism to non-relatives can also be explained away, in what has become a cottage industry within biology. An animal might care for the offspring of another that it is unrelated to because it hopes to obtain the same benefits for itself later on (a phenomenon known as reciprocal altruism). The hunter who generously shares his spoils with others may be doing so in order to signal his superior status to females, and ultimately boost his breeding success. These apparently selfless acts are therefore disguised acts of self-interest.

All of these examples fit economists' arguments that *Homo sapiens* is also *Homo economicus*—maximising something that economists call utility, and biologists fitness. But there is a residuum of human activity that defies such explanations: people contribute to charities for the homeless, return lost wallets, do voluntary work and tip waiters in restaurants to which they do not plan to return. Both economic rationalism and natural selection offer few explanations for such random acts of kindness. Nor can they easily explain the opposite: spiteful behaviour, when someone harms his own interest in order to damage that of another. But people are now trying to find answers.

Good for you, good for me

The favoured tools for exploring seemingly odd behaviours are called public-goods experiments and ultimatum games. In a public-goods experiment, each member of a group of subjects is given a financial stake and asked to use this money to contribute to a common pool. This pool is then expanded by the

experimenters and redistributed to individuals in the group.

One recent public-goods experiment was conducted by Ernst Fehr from the University of Zurich and Simon Gächter at the University of St Gallen in Switzerland. Sets of four students were given around $20 to participate in a group project. They were told that they could keep any money they did not invest. The rules of the game were that every $1 invested would yield $1.60, but that these proceeds would be distributed to all group members—in other words everyone would get 40 cents. Thus if everyone invested, each would walk away with $32, and the public good would have been served. If, however, only one person invested, that sucker would take home a mere $8.

The experiment was run first as a series of six rounds in which the participants were anonymous, investment decisions were taken simultaneously, and no two participants interacted more than once. At the end of each round, each player was told how other members of the group had invested and what the individual pay-offs would be. In this version of the game, people quickly learned not to invest. By the sixth round, contributions to the pool had dwindled to nothing.

The second version of the experiment, though, gave the individuals the opportunity to punish each other financially at the end of each investment round. At a cost of $1, a group member could anonymously fine another $3. Of the 240 participants in the experiment, 84% punished at least once and around 9% punished more than ten times. Most punishment was imposed by above-average contributors (deemed co-operators) on below-average contributors (deemed defectors or free-riders). Punishment was related to notions of fairness; the amount of punishment given was directly related to how far a free-rider's contributions deviated from the group's average. And punishment had an effect. It substantially increased the amount that was invested in the public good: more than 90% of the participants contributed more money when punishment was a possibility.

These punishments might look spiteful. In fact, they were altruistic. This is because, at the end of each investment round, the participants were swapped between groups so they would never invest with the same people again. Participants were therefore paying to punish someone with whom they would not interact again. Altruism, in other words, emerged in the second form of the game, as punishment, but not in the first.

The idea that people sometimes value “fairness” over personal gain was also suggested by an ultimatum game run last year by Joseph Henrich, an anthropologist at the University of Michigan's business school, and his colleagues. In an ultimatum game, a participant is given what is for him the equivalent of a day's wages, and asked to contribute a portion of this to a second, anonymous person whom he will never meet again. The recipient can accept or reject this offer, but if he rejects it, neither party receives any money.

The logic behind an ultimatum game suggests that, if people wish to maximise their resources, as standard economics assumes, a recipient will accept any offer made by a donor. Conversely, the donor will always offer as little as possible. But that is not how things turn out. Offers are guided by notions of what is fair, as are rejections. The researchers found that offers ranged from 22% to 58%, and offers higher than 50% were sometimes rejected.

This evidence and the findings of public-goods experiments led the anthropologists to conclude that acceptance and rejection were strongly linked to feelings of fairness and reciprocity in addition to material benefits. People reward those who act in a co-operative manner and punish those who do not—even if such behaviour costs them something personally.

That is, of course, only a scientific confirmation of a human commonplace. And when a new phenomenon is recognised by science, a name always helps. In a forthcoming paper in *Human Nature*, Dr Fehr and his colleagues argue for a behavioural propensity they call “strong reciprocity”. This name is intended to distinguish it from reciprocal altruism. According to Dr Fehr, a person is a strong reciprocator if he is willing to sacrifice resources to be kind to those who are being kind, and to punish those who are being unkind. Significantly, strong reciprocators will behave this way even if doing so provides no prospect of material rewards in the future.

Turn and face the change

That does not, of course, explain how strong reciprocity evolved in the first place. The modern theory of natural selection sees the process working on individuals: if you are “selected out” (ie, killed), your genes

cannot contribute to the next generation. Most selective pressures (predators, sexual competitors and so on) work at the individual level. Those that might wipe out whole groups at a time, such as infectious diseases, are not susceptible to collective action, so might as well be individual pressures. However, if what kills individuals frequently kills entire groups, but is something that collective action might successfully combat, the unit of selection might become the group. In the case of human beings, who (thanks to language) can collaborate in detail, a wide range of group-threatening risks—wars, famine, environmental catastrophes and so on—might be susceptible to such collective action. Groups containing strong reciprocators might be better adapted to survive, particularly since their behaviour coerces even the selfish into action that favours the common good. Genes for strong reciprocity would thus spread.

The idea of strong reciprocity explains both previously inexplicable altruistic acts and the existence of spite. That makes it theoretically attractive. Its boosters also think that it might have practical applications. A pair of economists, Samuel Bowles at the Santa Fe Institute in New Mexico and Herbert Gintis of the University of Massachusetts in Amherst, has suggested that if policymakers want to achieve certain public goods, such as the sharing of common resources, it might be useful to provide opportunities for the public-spirited to punish the free-riders in society. This kind of thing works in small fishing communities, where free-riders are punished by social exclusion. Extending these sorts of penalties to society at large could pit the better side of human nature against its other half, and make things better for everyone.

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The Antarctic ice shelf

Breaking the ice

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The collapse of a large ice shelf is more striking than alarming

IS ANTARCTICA vanishing? The satellite image on the left shows the Larsen B ice shelf, part of the Antarctic Peninsula, as it was five weeks ago; the picture on the right shows the same spot a few days ago. The scale and speed of Larsen B's collapse have shocked climatologists. After 12,000 years of torpor, more than 500m tonnes of ice have crumbled into the sea in just a few weeks.

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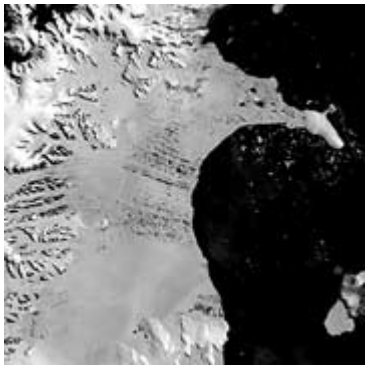

Before . . .

By itself, the collapse will not cause a rise in sea level. The ice shelf floated on the ocean's surface, so its disintegration will leave the oceans unaffected. But the event has scared environmentalists, because such shelves keep Antarctica's landlocked ice in check. If enough of these shelves collapsed and the glaciers melted, sea level could rise many metres.

David Vaughan of the British Antarctic Survey blames Larsen B's collapse on the unusual warmth of that part of Antarctica, where the temperature is rising five times faster than the rest of the planet. Reassuringly, however, he says that the ice shelves that do the brunt of the work in restraining the continent's glaciers lie in chillier regions of Antarctica. Moreover, some parts of the continent are cooling and in others the ice is thickening. So Larsen B's meltdown does not herald the deluge. But it does show that even glacial events can spring sudden surprises.

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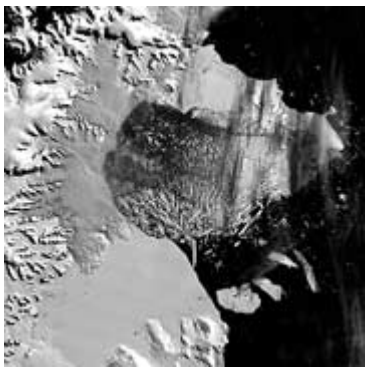

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Synthesising DNA

The gene machine

Mar 21st 2002 | SAN DIEGO
From The Economist print edition

An innovative way to make very long strands of DNA

IN A science-fiction movie called “Species”, a mysterious signal from outer space turns out to describe the genome of an unknown organism. When the inevitable mad scientist synthesises the DNA described by the instructions, the creature he breeds from it turns out to resemble Natasha Henstridge, an athletic actress. Unfortunately, the alien harbours within her lissom form the destructive powers of a Panzer division, and it all ends badly for the rash geneticist and his laboratory.

Glen Evans, chief executive of Egea Biosciences in San Diego, California, acknowledges ruefully that despite seeking his expert opinion—in return for which he was presented with the poster of the striking Ms Henstridge that hangs on his office wall—the producers of “Species” did not hew very closely to his suggestions about the feasibility of their script ideas. Still, they had come to the right man. Dr Evans believes that his firm will soon be able to create, if not an alien succubus, at least a tiny biological machine made of artificial proteins that could mimic the behaviour of a living cell.

Making such proteins will require the ability to synthesise long stretches of DNA. This is the molecule that carries a cell's genes, the instructions for stringing proteins together out of building blocks known as amino acids. Existing technology for synthesising DNA can manage to make genes that encode a few dozen amino acids, but this is too short to produce any interesting proteins. That means researchers must spend their days tweaking natural genes and studying the mutated proteins that result.

Egea's technology, by contrast, would allow biologists to manufacture genes wholesale. The firm's scientists can make genes long enough to encode 6,000 amino acids. They aim to synthesise a gene for 30,000 amino acids within two years—an amount of genetic material equivalent to the genome of the simplest living cell.

Using a library of the roughly 1,500 possible “motifs” or folds that a protein can adopt, Egea's scientists employ computers to design new proteins that are likely to have desirable shapes and properties. To synthesise the DNA that encodes these proteins, Egea uses a machine it has dubbed the “genewriter”. Dr Evans likens this device to a word-processor for DNA, on which you can type in the sequence of letters defining a piece of DNA and get that molecule out.

The genewriter's software parses the long DNA sequence into tiny, easily manufactured segments. Batches of each of these small pieces are synthesised and then set out in trays of small wells, rather like miniature egg cartons. A pipette-wielding robot combines the pieces into pairs by picking up a dollop of one piece and adding it to the next. To do this, the mixture is then cooked at a specific temperature with an enzyme known as a ligase so that the overlapping ends of the two pieces fuse together to make one longer piece of DNA. In the same way, this pair is then glued to another pair that corresponds to the next stretch of the desired molecule. Steadily, longer pieces are stuck together until the entire strand is complete.

The trick of this technique is designing the fragments of DNA in the way that gives them the best chance of sticking together correctly. The firm's scientists must also take care to control the gluing process to filter out botched joins along the way, so that the batches of growing DNA remain pure.

Once a strand is complete, it can be inserted into a chromosome so that the cells of an organism can manufacture the encoded protein. At this stage the genewriter can also act as a translator, rewriting DNA to take into account the slight variations in genetic language that exist between organisms. Most amino acids can be encoded by two or three different snippets of DNA, and species

By substituting bits of code, the genewriter makes it possible for a

have evolved to be choosy about which of these snippets they prefer. By substituting the bits of code that are most often used to encode particular amino acids in various species, the genewriter makes it possible for a gene developed and tested in a bacterium, say, to be tweaked so that a plant or an insect can read it efficiently.

gene to be tweaked so that a plant or an insect can read it efficiently

The genewriter also allows Egea to make variants of genes, which can help scientists to change and improve the function of proteins. One of Egea's early projects was to produce a spectrum of different colours by creating variations on a bacterial protein that fluoresces green. It is now pushing ahead with commercial applications. The American army has awarded it a contract to incorporate spider silk into fibrinogen, a molecule that causes blood to clot. The aim is to produce a battlefield glue with which soldiers could rapidly stop up their wounds. Several agricultural firms have commissioned Egea to improve the resistance to parasites of various crops by designing new genes that could be inserted into their genomes.

As Egea extends the length of DNA it can synthesise, Dr Evans envisages encoding not just proteins, but entire biochemical pathways, which are teams of proteins that conduct metabolic processes. A collection of such molecules could conceivably function as a miniature machine that would operate in the body and attack disease, just as the body's own defensive cells do. Perhaps Dr Evans and his colleagues ought to get in touch with their friends in Hollywood.

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The American civil war

Fighting for the lady

Mar 21st 2002
From The Economist print edition

Hulton Getty

The author of “Schindler's List” rakes over the life of a controversial American

THE title of this biography could hardly be more provocative. ThomasKeneally, an Australian writer, is unapologetic. In labelling a hero of the American civil war a notorious scoundrel he switches the spotlight from the braveactions of Dan Sickles at the battle of Gettysburg to his earlier premeditated murder in Washington, DC, of the lover of his young and pretty Italian-American wife, Teresa. It is not the murder itself that disgusts Mr Keneally but Sickles's treatment of his wife afterwards, and how his behaviour mirrored the hypocriticalmisogyny of 19th-century America.

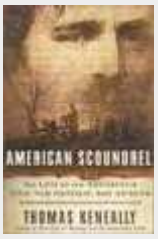
The murder victim, Philip Barton Key, Teresa Sickles's lover, came from a famous old southern family. He was the nephew of the then chief justice of the American Supreme Court and the son of the writer of the country's national anthem, “The Star-Spangled Banner”. Sickles, a Tammany Hall politician in New York turned Democratic congressman in Washington, shot Key dead in 1859 at a corner ofLafayette Square, within shouting distance of the White House.

The murder trial was melodramatic, even by the standards of the day. The jury was told that Sickles had armed himself with three guns and confronted his victim with the cry: “Key, you scoundrel, you have dishonoured my house—you must die!” Nonetheless, with the help of eight lawyers, Sickles was found not guilty after using the novel plea of “temporary insanity”. The country at large was just as forgiving, viewing Key's murder as a gallant crime of passion. Within three years, Sickles was a general on the Unionist side in the American civil war and, as a new friend of Abraham and Mary Lincoln, a frequent sleepover guest at the White House.

Mrs Sickles was less fortunate. She was shunned by friends she had made as the wife of a rising politician. Her husband, a serial adulterer whose many mistresses included Queen Isabella II of Spain and the madam of an industrial-sized New York whorehouse, refused to be seen in her company. Laura, the Sickles's daughter, was an innocent victim of her father's vindictiveness and eventually died of drink in the Bowery district of New York.

Sickles's bold actions at Gettysburg are, in their own way, just as controversial. Argument continues to

American Scoundrel: The Life of the Notorious Civil War General Dan Sickles
By Thomas Keneally



Doubleday/Nan A. Talese; 360 pages; $27.50. Chatto and Windus; £20

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rage among scholars, and between military buffs on civil war websites, as to whether he helped the Union to victory or nearly caused its defeat when he moved his forces out of line to occupy what he thought was better ground.

James Longstreet, the Confederate general who led the attack against the new position, was in no doubt about the brilliance of the move. In a letter to Sickles after the war, he wrote: “I believe it is now conceded that the advanced position at the peach orchard, taken by your Corps and under your orders, saved that battlefield to the Union cause.”

Mr Keneally remains sceptical. Longstreet and Sickles, he notes, were by then firm friends who seized every opportunity to inflate each other's reputation at the expense of their superiors at Gettysburg: Robert E. Lee for the Confederacy and George Meade for the Union. They also had their own gripes. Longstreet thought Lee had fought the wrong way in the wrong place. Sickles despised Meade's piety. He saw himself as a man's man and much preferred to serve under a bar-and-brothel general, like Joseph Hooker, the Union commander at Chancellorsville.

Mr Keneally is better known as a novelist. His books include “Schindler's List”, “Confederates” and “To Asmara”. But here he shows himself just as adept at biography, and achieves both his main aims. He restores the reputation of Teresa Sickles, “this beautiful, pleasant and intelligent girl”, and breathes full and controversial life into a famous military engagement.

American Scoundrel: The Life of the Notorious Civil War General Dan Sickles.
By Thomas Keneally.
Doubleday/Nan A. Talese; 360 pages; $27.50. Chatto and Windus; £20

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American politics

The Bushbaby grows up

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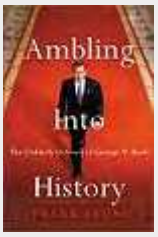
From The Economist print edition

IN THE weeks after September 11th, says Frank Bruni who covered George Bush's amble to the White House, if you asked an official in Washington how the president was feeling, he or she would instantly reply, “focused”. Then they would add how resolute he seemed. If you went elsewhere within the circle of those Republicans who might be presumed to see the president, they too would respond with the very same words: the president was, “Well, focused. Oh—and resolute.”

Mr Bruni's book, assembled from his contemporaneous notes, as the lawyers say, on the campaign plane and its attendant buses, is being hailed as an addition to the literature about Mr Bush, to put alongside Alexandra Pelosi's irreverent documentary, “Journeys with George”. Its real value, though, may be not so much in its insight into the president's distinctly quirky personality, as in its further evidence about the cynical media manipulation that is now taken almost for granted in presidential campaigns. The shelf it will end up on, perhaps, is not the one with glimpses of presidential psychology, like Judge Rosenman's “Working with Roosevelt” or Ben Bradlee's “Conversations with Kennedy”, but among the classic peeks behind the scenes, such as Joe McGinnis's “The Selling of the President” and Tim Crouse's “The Boys on the Bus”.

Ambling into History: The Unlikely Odyssey of George W. Bush
By Frank Bruni



HarperCollins; 278 pages; $23.95

Buy it at
Amazon.com
Amazon.co.uk

Mr Bruni is inclined to share, a little grudgingly, perhaps, the general judgment that Mr Bush has acquitted himself rather well in office over the last six months. He praises in particular his patience and his movement from unilateralist rhetoric to a new sensitivity to “the interlocked fates of free nations”. But his account of Mr Bush's behaviour, before his time of trial, certainly raises eyebrows.

The candidate comes across as jokey, slightly adolescent, even mildly neurotic. He used to go to great lengths to get back to his beloved Texas ranch, even at the cost of lengthy journeys between campaign appointments. He always travelled with his own personal pillow, in a large bag. He seemed almost flirtatious in his desire for affection from reporters and staff, in his invention of nicknames for them and his patting and touching, carefully reserved for male, not female journalists.

More interesting is the picture Mr Bruni paints of the campaign staff's obsessive desire to control the image that this rather relaxed candidate would present to newspaper readers and, especially, television viewers. Mr Bruni compares it to “a contrived pageant with pragmatic goals”:namely, to win the election at whatever cost. But Mr Bruni adds that “modern politics wasn't just superficial because the politicians made it so. It was superficial because the voters let it be.” Even now, “focused” and “resolute” are as nuanced as you'll get from those around him.

Reuters

George W. Resolute

Ambling into History: The Unlikely Odyssey of George W. Bush.
By Frank Bruni.
HarperCollins; 278 pages; $23.95

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About sponsorship

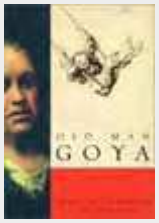
Francisco Goya

Old, deaf and happy

Mar 21st 2002
From The Economist print edition

FRANCISCO GOYA, who immortalised Spain's Bourbon royalty in paint, lived to a great age. In 1792, when he was 47, he became very ill. No one is sure what the cause was: it might have been a form of poisoning brought on by the lead-based white paint that he used, or a variation of Ménière's disease, or something else. There were rushing sounds in his ears, he said, and he often felt dizzy, faint and deaf. Goya could not amplify sound with the help of an ear trumpet. He could not, like Beethoven, hold one end of a stick clenched between his teeth and rest the end on top of the piano so that when the notes were played they were channelled directly into his skull. The attack lasted several weeks, and although he recovered, for the rest of his life he remained, as Julia Blackburn writes, “as deaf as a dead man who will not be woken from his cold sleep, no matter how loudly you shout.”

Old Man Goya
By Julia Blackburn



Pantheon Books; 240 pages; $23.
Jonathan Cape; £16.99

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Amazon.com
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Ms Blackburn likes writing fiction, and she is good at it. But her real talent lies in conjuring up lives lived elsewhere and long ago. Not since the unforgettable “The Emperor's Last Island” was published just over a decade ago, followed shortly after by “Daisy Bates in the Desert”, has she written so well.

In a brief note at the start of “Old Man Goya”, Ms Blackburn tells of her elderly mother's death just as she was getting started on Goya. Her mother's illness, the slow loss of her senses, her gradual separating of herself from the world permeate Ms Blackburn's thoughts as she sets about imagining Goya's transition from the royal portraitist who bought himself a patented gilded carriage made in England to the scruffy chronicler of humble daily life, with all its eating, whoring and masturbation during the hard years of the Peninsular war and the yellow fever that followed. Her imaginings are broken up with photographs of Goya's etching plates, his wartime “Desastres de la Guerra” and the more intimate “Caprichos”.

Ms Blackburn's chief interest is in examining how Goya's art, particularly the busy etchings (each of which he would do in the time it took him to smoke two cigarettes) was affected by his deafness. With one sense gone, how did the others compensate for the loss? How, for example, was he able to feel the noise of an Easter procession “seeping into the palms of his hands, rising through the bones of his feet”, so that “he could see it in the contorted faces of the people, their arms flailing with energy”? How could he make a drawing of a thin and dangerous man chattering to himself, of a mongoloid weeping, of two old people laughing, of three young girls whispering?

After his wife died Goya took up with a young mistress, much to the irritation of his only son, Javier, whose chief interest was in separating the old man from his wealth. Goya and the young Leocadia moved between Madrid and Bordeaux, where Goya painted and drew, happy not to understand the language for it meant not having to confess he was deaf. Signalling on his deathbed that he wished to write a new will to take care of Leocadia, the forgetful old man was assured falsely by his daughter-in-law that it had already been done. Goya was buried, according to his wishes, in the brown robes of his patron saint, Francis of Paolo, who owned nothing and needed nothing and who founded a religious order called the Minims, the least brethren.

Reading Ms Blackburn's work, you have the uncanny sensation that you have met Goya, felt his honest horny hands, watched him work. After his death, it took only a short time for Leocadia to be turned out of her home. Goya, you feel certain, would have been deeply angry.

Old Man Goya.

By Julia Blackburn.
Pantheon Books; 240 pages; $23.
Jonathan Cape; £16.99

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About sponsorship

Historical geography

Entering the monsoon world

Mar 21st 2002
From The Economist print edition

THE monsoons of maritime Asia are the world's oldest corridors of long-range commerce. Heroic voyages in search of profit or Buddhahood were the subjects of legend centuries before the Atlantic and Pacific were crossed.

When Vasco da Gama rounded the Cape of Good Hope in 1498, he opened direct access for Europe to India and the Arabian Gulf. From then on European merchants and imperialists invaded the Indian Ocean, grabbed much of its trade and began to take over its most valuable centres of production. How this happened is one of the mysteries of history. There is no shortage of theories: still lacking is detailed research to support or explode them. Valueless generalisations about the superiority or inferiority of western “individualism” and oriental “corporatism” infect inquiry. Quests for Weber-style socio-cultural explanations of economic fortunes leave most practitioners looking silly. Comparisons of the “proto-capitalism”, technical inventiveness, military prowess and value-systems of rival states and societies generate partisan rancour.

The Arabian Seas: The Indian Ocean World of the Seventeenth Century
By Rene J. Barendse

M.E. Sharpe; 512 pages; $34.95

Buy it at
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Amazon.co.uk

Rene Barendse's study of European traders in the western Indian Ocean and contiguous lands in the 17th century shows how detailed evidence helps. With every shake of the kaleidoscope the overall pattern becomes clearer. Mr Barendse's abundant use of Dutch archives enables him to trace individual peddlers from Samarkand to Sinkiang and Circassia. He visits neglected outposts of the system, such as Madagascar and the Comoros. He brings in women, whom he calls “the caryatids of empire”. He can show us just what kind of capitalism was practised by the famed Gujarati capitalists. He spies for us on meetings of Dutch price-fixers in Surat.

His book is a lightly-adapted dissertation and betrays the principal defect of the genre: it needs more editing. It also reveals the perhaps sensible reluctance of a prudent young scholar to draw radical conclusions from his discoveries. Mr Barendse fails to consider the influence of relations with indigenous states on the outcomes of intra-European rivalries, principally the Dutch and the British. Another recent Leiden University PhD thesis, by Ernst van Veen, is very good on this. And Mr Barendse's method, of dealing in turn with the European national communities, surrounds this work with a misleadingly old-fashioned air.

The Arabian Seas: The Indian Ocean World of the Seventeenth Century.
By Rene J. Barendse.
M.E. Sharpe; 512 pages; $34.95

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About sponsorship

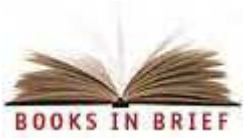
Genocide

How to stop the killing

Mar 21st 2002
From The Economist print edition

Trying mass killers is good. Preventing genocide would be better. But how easily?

Get article background



THROUGH the stories of thousands of victims, perpetrators, judges and soldiers—and the difficult search for justice offered by international tribunals—Elizabeth Neuffer gives a human face to the horrors of Bosnia and Rwanda and tries to understand how it all happened. She listens to Hasan Nuhanovic, a Bosnian student who lost his family at Srebrenica, as well as Witness JJ, whose testimony about rape in Rwanda made legal history, and General Romeo Dallaire, head of the UN peacekeeping force in Rwanda, who wept tears of rage in court, unable to forget that his repeated pleas for more troops and for the authorisation to step in were ignored. “All I needed was three battalions.”

MICHAEL BARNETT offers a chilling explanation of why the UN froze while about 800,000 Tutsis and Hutu moderates were hacked to death in Rwanda in 1994. Mr Barnett, a political officer in America's mission to the UN, blames an institutional culture which led the UN's well-intentioned staff to become entangled in conflicting interests and end up concluding that doing nothing was the proper way to proceed.

TO STOP history from repeating itself, Brian Lepard's guide offers a clear legal road map for humanitarian intervention. He draws principles from international law and religious texts to help interveners solve ethical conflicts between human rights and national sovereignty, the use of force and peaceful conflict resolution, or effective intervention and remaining impartial.

LAW, unfortunately, is only a small part of the problem of war crimes. Kenneth Campbell blames America's leaders for tying their own hands with the false

The Key to My Neighbour's House: Seeking Justice in Bosnia and Rwanda
By Elizabeth Neuffer

Bloomsbury; 528 pages; £18.99

Buy it at
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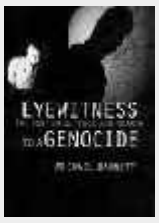
Amazon.co.uk

Eyewitness to a Genocide: The United Nations and Rwanda
By Michael Barnett



Cornell University Press; 240 pages; $25

Buy it at
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Amazon.co.uk

Rethinking Humanitarian Intervention
By Brian D. Lepard

Penn State University Press; 528 pages; $55

Buy it at
Amazon.com
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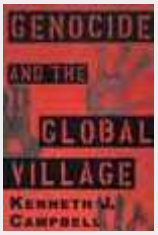
Genocide and the

assumption that a public that was traumatised by Vietnam and Somalia would now support fewer ventures in faraway lands. Worse, they have purposefully refrained from using the “G-word” for fear that something may have to be done about it. Mr Campbell argues that stepping in to prevent or stop genocide is more than a moral obligation: it is essential to the survival of a world order based on liberal values and the rule of law, and therefore a national interest.

BY FAILING to prevent and punish genocide over the last century, has America indirectly encouraged more atrocities? Are the intervention in Kosovo and Slobodan Milosevic's trial in The Hague signs that the lessons of the recent past are finally being learnt? Maybe, in both cases. But the reality is that America will likely remain torn between pressure to be a global policeman and accusations that it is thus a global bully.

Global Village
By Kenneth J. Campbell



Palgrave; 192 pages; $19.95 and £13.99

Buy it at
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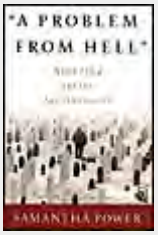
Amazon.co.uk

A Problem from Hell: America and the Age of Genocide
By Samantha Power



Basic Books; 610 pages; $30 and £21.99

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About sponsorship

Video art

Art for the MTV generation

Mar 21st 2002
From The Economist print edition

From radical to respectable in 30 years

IT IS surely fitting that the Tuscan town of Vinci, birthplace of Leonardo and home to a museum of his machines, should put on a show of the television-robot sculptures of Nam Jun Paik. This Korean-born American artist and the Renaissance master are kindred spirits: Leonardo saw humanistic potential in his scientific experiments, Mr Paik seeks to harness media technology for artistic purposes. A pioneer of video art in the late 1960s, he treats television as a space for art images and as material for robots and interactive sculptures.

Nam Jun Paik: Museo Leonardiano, Vinci, until 16 June.

First Decade: Video from EAI Archives: MoMA, New York, until April 30th.

Bill Viola: Deutsche Guggenheim, Berlin, until May 5th.

New Ocean travels to Tokyo in September and to the Fondazione Re Rebaudengo per l'Arte, Turin, in January 2003.

Shirin Neshat: Castello di Rivoli, Turin, until May 5th.

Mr Paik was not alone. He and fellow artists such as Bruce Nauman and Vito Acconci picked on the video cameras because they offered an easy way to record their performance art. Now, to mark video art's coming of age, New York's Museum of Modern Art (MOMA) is looking back at their efforts in a film series called “The First Decade”. It celebrates the early days of video by screening the archives of Electronic Arts Intermix (EAI), one of the world's leading distributors of video and new media art, founded 30 years ago.

One of EAI's most famous alumni is Bill Viola. Part of the second generation of video artists, who emerged in the 1970s, Mr Viola experimented with video's expressive potential. He has been called the Rembrandt of the genre and is regarded as the most painterly of video artists. His camera explores religious ritual and universal ideas. The Viola show at the Deutsche Guggenheim in Berlin shows usmoving-image frescoes that cover the gallery walls and envelop the viewer in all-embracing cycles of life and death.

Like him, Gary Hill, another Old Master of video art, is phenomenally popular. Both use the screen as a two-dimensional canvas in essentially traditional ways. But a new generation has sprung up, for whom video is second nature—they grew up with MTV, the music-video channel, which is now 20 years old—and they are taking video art in new directions.

One new star is a Californian, Doug Aitken, who took over London's Serpentine Gallery last October with an installation called “New Ocean”. Some say Mr Aitken is to video what Jackson Pollock was to painting. He drips his images from floor to ceiling, creating sequences of rooms in which the space surrounds the viewer in hallucinatory images, of sound and light.

At the Serpentine, Mr Aitken created a collage of moving images, on the theme of water's flow around the planet as a force of life. “I wanted to create a new topography in this work, a liquid image, to show a world that never stands still,” he says. The boundary between the physical world and the world of images and information, he thinks, is blurring.

In “New Ocean”, figures move in and out of random locations around the world: each time the camera pulls out, they enter a different place, on a different screen, never lingering long enough to build a narrative. Both frustrating and mesmerising to watch, the work evokes nomadic displacement. Some critics have called this piece more beautiful than meaningful, lacking conceptual depth. But Mr Aitken has no fixed agenda. His video environments comment on globalisation and nature, and can be seen as a romantic attempt to picture the

world in new ways. His work is described in “Doug Aitken” (Phaidon, 2001).

Evocation of atmosphere pervades the work of an Iranian-born, New York-based artist, Shirin Neshat. She had a big retrospective in Montreal last year and currently has a show in the baroque spaces of the Castello di Rivoli, outside Turin. The artist, who left Iran in 1974 to study at the University of California, Berkeley, stayed in the United States after the Islamic revolution of 1979 and launched her career with dramatic photographs that explored the theme of women and Islam.

In the mid-1990s, however, she switched from photography to film and video because she believed that the cinematic medium allowed her greater flexibility in portraying the roles allotted to men and women in Islam. “When you have only a single image, the message you convey may be like propaganda, whereas when you use film, you can become a storyteller, choreographing ideas and images, creating non-linear narratives,” Ms Neshat says. “I weave messages into my work that can't be pinned down, like a dream. I want to insist on the complexity of women who wear the veil.”

While Ms Neshat films her work before transferring it to video for museum installations, like Mr Aitken she records original soundtracks, which reverberate like a mantra. Her most famous work, “Turbulent”, which won the Golden Lion at the 1999 Venice Biennale, is a two-screen installation in which distinct images echo the separate worlds of men and women in Islam. On one screen, a man sings a love song by a great 13th-century Persian poet, Rumi, to a crowded auditorium of men. As he bows, a female singer on the screen opposite begins to chant a primal, almost pre-musical song, whirling in a trance before an empty auditorium (women in Iran are forbidden to sing in public). Viewers must turn from one to the other, unable to see both at once.

The interplay of illusion and reality, sound and image, references to art history, politics, film and television in this art form that is barely 30 years old can make video art difficult to define. Many call it film-based or moving-image art to include artists who work with other cinematic media. Critics of video art have accused it of voyeurism, of navel-gazing, of being hermetic. But at its best, the appeal of video art lies in its versatility, its power to capture the passing of time and on its ability to communicate both inside and outsidegallery walls.

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About sponsorship

Walter Rockler

Mar 21st 2002
From The Economist print edition

Walter Rockler, a prosecutor at Nuremberg, died on March 8th, aged 81

AP

WHAT people seemed to find most interesting in Walter Rockler's long career as a lawyer was that he had taken part in the Nuremberg trials. What were the Nazis really like, he would be asked, Hitler, Goering and that lot? Hitler never stood trial, he would patiently remind those whose knowledge of history many years before they were born was a bit fuzzy. Goering stood trial and committed suicide. Ten other defendants were hanged. But, Mr Rockler would add, he never saw Goering and co. Their trials were disposed of in 1946, shortly after the end of the second world war. Mr Rockler arrived in Germany in 1947.

He had answered an advertisement for lawyers to prosecute a second group of defendants, those accused of collaborating in war crimes. During the war Mr Rockler had served as a marine in the Pacific and had learnt Japanese. He suggested that he might be sent to Tokyo to prosecute Japanese war criminals. But the Japanese trials were coming to an end, and Douglas MacArthur, Japan's American overlord, was not keen to prolong the agony. In Germany thousands still awaited the victors' justice. Walter Rockler, a recent graduate of Harvard University's law school, was provided with a German phrase book and dispatched forthwith.

For two years he took part in trials of bankers and industrialists who had had a hand in the systematic murder of millions of people and in the illegal pursuit of war. In 1995, at a conference to mark the 50th anniversary of the start of the trials, he expressed mixed feelings about their value. Was it that Nuremberg law was created *ex post-facto* to suit the passion and clamour of the time, a view that had been expressed by William Douglas, a member of the Supreme Court? No, it wasn't that exactly. Although some had criticised the trials, they had an important symbolic value. But they had had no substantial impact, Mr Rockler said. “Wars and savagery have not been deterred.” There had been frequent violations of the Nuremberg judgment that “no political or economic situation” can justify initiating a war of aggression, and he believed they would continue. Worse, the violators had included the United States, which had taken the lead in setting up the Nuremberg trials.

A visit to Russia

Walter Rockler was not by nature a rebel. After leaving Germany he made tax law his main expertise, practising it in Chicago, New York and latterly for 36 years in Washington. He had a brief break from private practice in the 1970s when Henry Kissinger, then secretary of state, asked him to go to Moscow to examine a Soviet dossier on possible Nazi-sympathisers in the United States. Mr Rockler was more intrigued by the prospect of visiting the Russia from which his parents had emigrated than of talking to the KGB. Nevertheless, on his return to the United States he dutifully accepted the directorship of a new unit set up by the government to find American Nazis. Nothing much came from his Nazi hunt, and he left the unit after two years to resume his tax battles with the Internal Revenue Service.

However, reawakened memories of the Nuremberg trials eventually turned Mr Rockler into a critic of American foreign policy. His concern came to a head with the bombing of Yugoslavia by American aircraft acting for NATO. In May 1999 he sent a letter to the *Chicago Tribune*, the newspaper of the town where he grew up and where he received his education before going to Harvard. It said in part

> The attack on Yugoslavia constitutes the most brazen international aggression since the Nazis attacked Poland to prevent “Polish atrocities” against Germans. The United States has

> discarded pretensions to international legality and decency, and embarked on a course of raw imperialism run amok...When we, the self-anointed rulers of the planet, issue an ultimatum to another country, it is “surrender or die”. To maintain our “credibility”, we must crush any semblance of resistance to our dictates to that country.

Strong words. Even so, in a world where millions upon millions of words are published each day, Mr Rockler was surprised by the impact of a letter in a local paper. As it was republished hither and thither he found himself a hero of liberals in America and Europe, a new personality on television, a guest on the campus circuit, always introduced as a former prosecutor at Nuremberg. “Who gave us the authority to run the world?” he demanded of an audience at Princeton University. Bill Clinton had violated the constitution by declaring war, a power entrusted to a “supine Congress, fascinated only by details of sexual misconduct”.

Criticism of Mr Rockler was muted. It was difficult to knock an obviously respectable and intelligent man just because he was letting off steam. What he did do was to create a debate about the importance of the Nuremberg judgment. How do you define “a war of aggression”? Could it be in some circumstances a defensive war? Discuss.

The United States is now engaged, under another president, in another war. What would Walter Rockler have said about that? No one knows. For some time Mr Rockler had been battling against lung cancer, and lost.

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Output, demand and jobs

Mar 21st 2002
From The Economist print edition

kp

% change at annual rate

	GDP 1 qtr	GDP 1 year		The Economist poll GDP forecasts 2002	2003	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		year ago
Australia	+ 5.2	+ 4.1	Q4	+ 3.4	+ 3.7	+ 0.4	Q3	+ 4.8	Q4	6.6	Feb	6.6
Austria	– 0.3	+ 0.9	Q3	+ 1.1	+ 2.4	– 3.3	Dec	– 3.5	Dec	3.7	Feb	3.4
Belgium	– 0.8	+ 0.1	Q4	+ 1.1	+ 2.9	– 7.5	Jan	– 2.0	Dec	10.8	Feb*	10.6
Britain	+ 0.1	+ 1.7	Q4	+ 1.9	+ 2.9	– 5.2	Jan	+ 5.9	Feb	5.1	Jan†	5.2
Canada	+ 2.0	+ 0.9	Q4	+ 1.7	+ 3.7	– 5.5	Dec	+ 5.7	Dec	7.9	Feb	6.9
Denmark	+ 0.7	+ 0.7	Q4	+ 1.4	+ 2.3	– 1.7	Jan	+ 1.4	Dec	5.0	Jan	5.3
France	– 0.6	+ 0.9	Q4	+ 1.4	+ 2.9	– 1.3	Jan	– 2.8	Jan	9.0	Jan	8.9
Germany	– 1.0	– 0.1	Q4	+ 0.7	+ 2.5	– 5.1	Dec	– 1.8	Jan	9.6	Feb**	9.3
Italy	– 0.8	+ 0.7	Q4	+ 1.2	+ 2.8	– 3.4	Jan	– 0.8	Dec	9.3	Oct	10.0
Japan	– 4.5	– 1.9	Q4	– 1.2	+ 1.1	–11.5	Jan	– 3.8	Jan	5.3	Jan	4.8
Netherlands	nil	+ 0.4	Q4	+ 1.2	+ 2.9	– 3.9	Jan	+ 1.2	Nov	1.9	Feb§	2.3
Spain	+ 0.7	+ 2.3	Q4	+ 1.9	+ 3.2	– 0.1	Jan	na		12.8	Jan	13.4
Sweden	+ 1.4	+ 1.1	Q4	+ 1.4	+ 2.8	– 4.3	Jan	+ 1.7	Jan	4.0	Feb*	4.2
Switzerland	+ 0.1	+ 0.4	Q4	+ 1.0	+ 2.0	+ 1.9	Q3	+ 3.8	Jan	2.6	Feb*	1.9
United States	+ 1.4	+ 0.4	Q4	+ 1.7	+ 3.6	– 4.1	Feb	+ 5.4	Jan	5.5	Feb	4.2
Euro area	– 0.8	+ 0.6	Q4	+ 1.2	+ 2.8	– 4.1	Dec	+ 0.4	Dec	8.4	Jan	8.5
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	– 1.8	– 0.9	Q4	na	na	–10.0	Jan	+ 4.5	Nov	9.4	Feb*	9.8
Greece	na	+ 3.7	Q4	na	na	– 4.0	Dec	+ 6.8	Dec	na		na
Iceland	na	+ 3.6	2000	na	na	+ 2.5	2000	na		1.8	Dec	1.3
Ireland	na	+ 3.2	Q3	na	na	+14.3	Jan	+ 9.1	Dec	4.2	Feb	3.6
Luxembourg	na	+ 8.5	2000	na	na	– 9.2	Dec	+10.0	Oct	2.7	Dec	2.6
New Zealand	+ 2.8	+ 2.1	Q3	na	na	+ 2.6	Q3	+ 7.4	Q4	5.4	Q4	5.6
Norway	+ 1.0	+ 1.8	Q4	na	na	+ 2.0	Jan	+ 2.5	Jan	3.3	Q4	3.1
Portugal	– 1.0	+ 1.3	Q3	na	na	+ 0.8	Jan	– 2.4	Jan	4.1	Q4*	3.8

*Not seasonally adjusted. †Nov-Jan; claimant count rate 3.1% in Feb. §Dec-Feb. **EU harmonised rate 8.1% in Feb.

Text refers only to the first 16 countries listed

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Prices and wages

Mar 21st 2002
From The Economist print edition

kp

% change at annual rate

	Consumer prices			The Economist poll consumer prices forecast		Producer prices			Wages/earnings		
	latest		year ago	2002	2003	latest		year ago	latest		year ago
Australia	+ 3.1	Q4	+ 5.8	+ 2.5	+ 2.3	– 0.7	Q4	+ 8.4	+ 4.9	Q4	+ 5.4
Austria	+ 1.9	Feb	+ 2.6	+ 1.6	+ 1.7	– 0.6	Feb	+ 2.6	+ 2.5	Feb	+ 2.6
Belgium	+ 2.6	Feb	+ 2.3	+ 1.6	+ 1.6	– 1.6	Jan	+ 5.9	+ 3.1	Q4	+ 1.6
Britain	+ 1.0	Feb	+ 2.7	+ 2.0	+ 2.4	– 0.3	Feb	+ 1.3	+ 2.7	Jan	+ 4.6
Canada	+ 1.3	Jan	+ 3.0	+ 1.2	+ 1.9	– 1.2	Jan	+ 3.2	+ 3.5	Dec	+ 0.8
Denmark	+ 2.5	Feb	+ 2.4	+ 1.8	+ 2.0	nil	Feb	+ 3.4	+ 4.1	Q4	+ 3.8
France	+ 2.0	Feb	+ 1.4	+ 1.2	+ 1.3	– 1.2	Jan	+ 3.6	+ 4.1	Q3	+ 5.3
Germany	+ 1.7	Feb	+ 2.6	+ 1.3	+ 1.4	– 0.5	Feb	+ 3.7	+ 2.3	Jan	+ 2.5
Italy	+ 2.5	Feb	+ 3.0	+ 1.8	+ 1.8	– 1.2	Jan	+ 5.4	+ 2.8	Dec	+ 1.7
Japan	– 1.4	Jan	– 0.3	– 1.0	– 0.5	– 0.1	Feb	+ 0.1	– 3.4	Jan	+ 0.2
Netherlands	+ 3.8	Feb	+ 4.5	+ 2.7	+ 2.3	– 2.6	Jan	+ 6.7	+ 3.8	Jan	+ 4.4
Spain	+ 3.1	Feb	+ 3.8	+ 2.3	+ 2.4	+ 0.1	Jan	+ 3.9	+ 3.6	Q3	na
Sweden	+ 2.8	Feb	+ 1.6	+ 2.0	+ 2.0	– 0.5	Jan	+ 3.0	+ 3.2	Dec	+ 2.7
Switzerland	+ 0.7	Feb	+ 0.8	+ 0.6	+ 0.9	– 1.5	Feb	+ 0.8	+ 1.3	2000	+ 0.3
United States	+ 1.1	Jan	+ 3.7	+ 1.3	+ 2.1	– 2.6	Feb	+ 4.0	+ 3.7	Feb	+ 4.1
Euro area	+ 2.4	Feb	+ 2.3	+ 1.6	+ 1.6	– 0.9	Jan	+ 4.8	+ 2.9	Q3	+ 2.5
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 1.8	Feb	+ 2.7	na	na	– 1.4	Feb	+ 3.2	+ 4.3	Q4	+ 5.0
Greece	+ 3.4	Feb	+ 3.5	na	na	+ 2.4	Dec	+ 6.7	na		na
Iceland	+ 8.7	Mar	+ 3.9	na	na	+ 8.7	Mar	+ 6.0	+ 9.8	Feb	+ 8.2
Ireland	+ 4.7	Feb	+ 5.3	na	na	nil	Dec	+ 4.5	+ 8.7	Q3	+ 7.4
Luxembourg	+ 2.3	Feb	+ 2.9	na	na	– 2.1	Dec	+ 5.0	+ 3.4	Aug	+ 7.0
New Zealand	+ 1.7	Q4	+ 4.0	na	na	+ 1.8	Q4	+10.7	+ 2.2	Q4	+ 1.6
Norway	+ 0.8	Feb	+ 3.6	na	na	–11.5	Feb	+ 3.8	+ 4.5	Q4	+ 4.3
Portugal	+ 3.2	Feb	+ 4.8	na	na	– 6.1	Jan	+ 7.3	+ 2.4	Apr	na

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Denmark

Mar 21st 2002
From The Economist print edition

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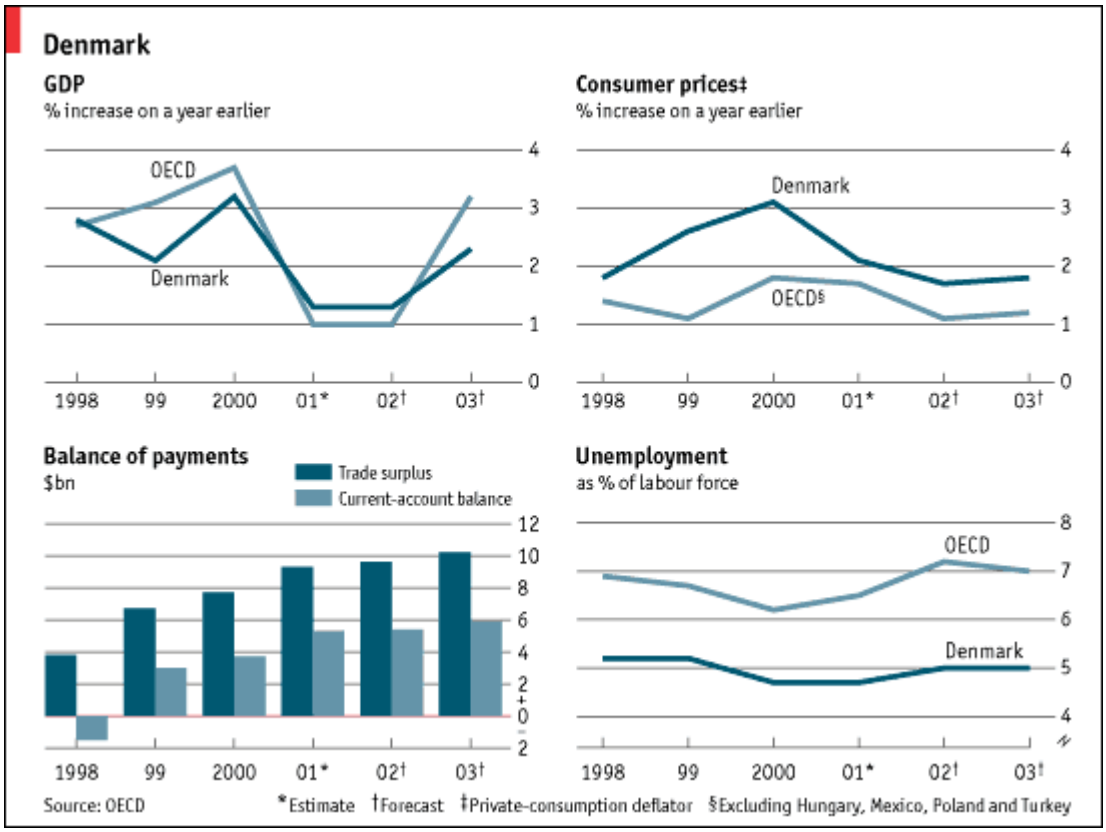

The Danish economy was growing at near to capacity when the world economic downturn struck. Growth last year was down to about 1.3%, says the OECD in a recent survey, and activity is expected to stay weak before accelerating in the middle of this year. The OECD says that Denmark's fiscal system could do with some reforms. Local governments have raised income taxes above nationally agreed levels, acting against the government's efforts to improve work incentives. It might be better to allow local governments to vary personal income-tax allowances rather than tax rates. Labour supply could be encouraged by reducing marginal labour-tax rates, and more could be done make Denmark's large public sector more efficient, perhaps by introducing more competition in the supply of public services.

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Money and interest rates

Mar 21st 2002
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	Money supply* % change on year ago			Interest rates % p.a. (Mar 20th 2002)					
				3-mth money market		2-year	10-year gov't bonds		corporate
	narrow	broad		latest	year ago	gov't bonds	latest	year ago	bonds
Australia	+21.6	+14.7	Jan	4.56	5.10	5.26	6.33	4.99	7.08
Britain	+ 7.1	+ 6.2	Feb	4.09	5.50	4.89	5.27	4.60	6.35
Canada	+17.7	+ 5.1	Jan	2.05	4.94	4.08	5.77	5.22	7.06
Denmark	+ 6.8	+ 8.7	Jan	3.70	5.00	4.49	5.36	4.90	7.05
Japan	+19.4	+ 3.7	Feb	0.06	0.08	0.05	1.45	1.05	1.56
Sweden	+ 7.1	+ 6.2	Nov	4.12	4.03	5.08	5.56	4.64	5.77
Switzerland	+ 7.5	+ 4.6	Feb	1.70	3.44	2.65	3.58	3.27	4.65
United States	+ 7.6	+10.9	Feb	1.88	4.63	3.65	5.40	4.77	7.06
Euro area†	+ 6.6	+ 7.9	Jan	3.38	4.77	4.06	5.13	4.60	5.77

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. † Germany for bonds. Benchmarks: US 30-year 5.82%, Japan No.237 1.45%. Central bank rates: US fed funds 1.75%, ECB refinancing 3.25%, BOJ overnight call 0.002%, BOE repo 4.00%. Sources: Commerzbank, Danske Bank, J.P. Morgan Chase, Royal Bank of Canada, Stockholmsbörsen, UBS Warburg, DRI-WEFA, Westpac, Thomson Financial Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Mar 21st 2002
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1995=100

	Mar 12th	Mar 19th*	% change on one month	% change on one year
Dollar index				
All items	70.0	70.7	+ 4.8	+ 0.8
Food	70.3	70.6	+ 3.6	+ 1.7
Industrials				
All	69.6	70.8	+ 6.4	- 0.4
Nfa†	69.2	70.2	+ 6.4	+ 5.8
Metals	69.9	71.4	+ 6.4	- 5.1
Sterling index				
All items	78.2	78.3	+ 5.1	+ 1.1
Euro index				
All items	105.4	105.3	+ 3.7	+ 3.1
Yen index				
All items	95.9	99.1	+ 3.4	+ 8.4
Gold				
$ per oz	293.20	293.35	- 1.6	+12.8
West Texas Intermediate				
$ per barrel	24.36	24.96	+20.6	- 3.0

* Provisional. † Non-food agriculturals.

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Stockmarkets

Mar 21st 2002
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Market indices

	Mar 20th	2002 high	2002 low	% change on one week	% change on record high	% change on Dec 31st 2001 in local currency	% change on Dec 31st 2001 in $ terms
Australia (All Ordinaries)	3,411.8	3,440.0	3,331.2	+ 0.5	- 0.8	+ 1.5	+ 5.4
Austria (ATX)	1,240.5	1,245.2	1,114.4	+ 0.6	-28.6	+ 8.8	+ 8.1
Belgium (Bel 20)	2,726.3	2,811.1	2,622.4	+ 0.9	-26.0	- 2.0	- 2.6
Britain (FTSE 100)	5,266.9	5,323.8	5,024.1	- 0.1	-24.0	+ 0.9	- 1.1
Canada (Toronto Composite)	7,915.4	7,958.1	7,418.1	+ 0.7	-30.5	+ 3.0	+ 4.1
Denmark (KBX)	229.2	231.3	216.8	+ 1.0	-24.1	+ 2.0	+ 1.3
France (SBF 250)	3,032.0	3,054.0	2,782.5	+ 1.8	-30.9	+ 1.7	+ 1.0
(CAC 40)	4,603.8	4,682.8	4,239.0	+ 1.8	-33.5	- 0.4	- 1.1
Germany (Xetra DAX)	5,364.7	5,462.6	4,745.6	+ 2.3	-33.5	+ 4.0	+ 3.3
Italy (BCI)	1,490.5	1,496.5	1,344.9	+ 1.1	-31.7	+ 4.0	+ 3.3
Japan (Nikkei 225)	11,526.8	11,919.3	9,420.9	+ 1.0	-70.4	+ 9.3	+ 9.0
(Topix)	1,097.9	1,125.4	922.5	+ 2.1	-61.9	+ 6.4	+ 6.0
Netherlands (AEX)	521.9	526.8	478.3	+ 2.1	-25.6	+ 3.0	+ 2.3
Spain (Madrid SE)	840.5	847.4	773.2	+ 2.2	-26.7	+ 2.0	+ 1.3
Sweden (Affarsvarlden Gen)	222.3	236.8	209.9	- 2.2	-44.5	- 4.0	- 1.2
Switzerland (Swiss Market)	6,612.1	6,630.0	6,105.2	+ 1.8	-21.4	+ 3.0	+ 3.3
United States (DJIA)	10,501.6	10,635.3	9,618.2	nil	-10.4	+ 4.8	+ 4.8
(S&P 500)	1,151.9	1,172.5	1,080.2	- 0.2	-24.6	+ 0.3	+ 0.3
(Nasdaq Comp)	1,832.9	2,059.4	1,716.2	- 1.6	-63.7	- 6.0	- 6.0
Europe (FTSE Eurotop 300)*	1,265.2	1,278.4	1,185.5	+ 0.8	-25.8	+ 0.3	- 0.3
Euro area (FTSE Ebloc 100)*	1,110.4	1,125.1	1,013.0	+ 1.4	-28.4	- 0.2	- 0.8
World (MSCI)†	1,011.4	1,024.4	937.0	+ 0.5	-30.2	na	+ 0.8
World bond market (Salomon)‡	435.7	443.1	430.3	- 0.1	- 5.3	na	- 0.9

*In euro terms. †Morgan Stanley Capital International index includes individual markets listed above plus eight others, in dollar terms. ‡Salomon Smith Barney World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Mar 21st 2002
From The Economist print edition

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	Trade balance*, $bn latest 12 months		Current account $bn latest 12 mths		The Economist poll % of GDP, forecast 2002	2003	Exchange rate trade-weighted† Mar 20th	year ago	Currency units per $ Mar 20th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2001‡
Australia	+ 2.1	Jan	− 9.2	Q4	− 3.2	− 3.3	75.8	69.2	1.88	2.03	2.68	1.67	1.43	0.1
Austria	− 4.3	Dec	− 3.6	Jan	− 2.1	− 1.9	100.2	100.4	1.13§	1.11	1.61	–	0.86	nil
Belgium	+ 11.2	Dec	+ 12.4	Sep	+ 4.6	+ 4.5	98.9	99.2	1.13§	1.11	1.61	–	0.86	nil
Britain	− 46.7	Jan	− 17.7	Q3	− 2.0	− 2.1	106.0	105.0	0.70	0.70	–	0.62	0.53	1.1
Canada	+ 39.0	Jan	+ 18.9	Q4	+ 2.1	+ 2.2	76.5	76.4	1.58	1.57	2.25	1.40	1.20	2.8
Denmark	+ 7.1	Jan	+ 4.2	Jan	+ 2.4	+ 2.3	101.9	102.1	8.40	8.32	12.0	7.43	6.39	2.0
France	+ 4.2	Jan	+ 26.8	Dec	+ 1.7	+ 1.7	101.5	101.8	1.13§	1.11	1.61	–	0.86	-1.5
Germany	+ 87.9	Jan	+ 15.4	Jan	+ 0.1	+ 0.2	98.5	98.9	1.13§	1.11	1.61	–	0.86	-2.5
Italy	+ 8.7	Dec	+ 3.2	Dec	+ 0.2	nil	72.4	72.7	1.13§	1.11	1.61	–	0.86	-1.4
Japan	+ 72.2	Jan	+ 91.1	Jan	+ 2.3	+ 2.3	128.5	136.9	132	123	188	116	–	-6.4
Netherlands	+ 21.4	Dec	+ 11.8	Q4	+ 3.7	+ 4.0	97.8	98.1	1.13§	1.11	1.61	–	0.86	1.1
Spain	− 38.5	Dec	− 15.2	Dec	− 2.2	− 1.9	74.2	74.3	1.13§	1.11	1.61	–	0.86	nil
Sweden	+ 12.9	Jan	+ 7.4	Jan	+ 2.4	+ 2.5	77.4	76.3	10.19	10.24	14.5	9.02	7.75	3.8
Switzerland	+ 1.6	Jan	+ 25.4	Q3	+10.1	+10.1	112.8	107.8	1.66	1.71	2.36	1.46	1.26	na
United States	−421.2	Jan	−417.4	Q4	− 4.1	− 4.3	122.3	119.5	–	–	1.43	0.88	0.76	0.6
Euro area	+ 43.4	Dec	− 15.6	Dec	+ 0.2	+ 0.2	78.6	79.3	1.13	1.11	1.61	–	0.86	-1.2
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 12.4	Jan	+ 8.2	Jan	na	na	77.9	78.4	1.13§	1.11	1.61	–	0.86	3.7
Greece	− 19.1	Nov**	− 7.3	Nov	na	na	57.5	57.5	1.13§	1.11	1.61	–	0.86	0.2
Iceland	nil	Jan	− 0.7	Q3	na	na	na	na	101	88	143	89.0	76.5	-0.2
Ireland	+ 31.4	Dec	− 1.2	Q3	na	na	87.3	87.7	1.13§	1.11	1.61	–	0.86	3.2
Luxembourg	− 2.8	Dec	+ 0.4	Q3	na	na	98.9	99.2	1.13§	1.11	1.61	–	0.86	5.3
New Zealand	+ 0.3	Jan	− 0.2	Q3	na	na	85.7	79.7	2.26	2.41	3.22	2.00	1.72	1.3
Norway	+ 24.1	Feb	+ 23.8	Dec	na	na	98.9	94.4	8.73	9.06	12.4	7.72	6.64	14.3
Portugal	− 14.0	Nov	− 10.5	Dec	na	na	89.2	89.5	1.13§	1.11	1.61	–	0.86	-1.7

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †1990=100, Bank of England. ‡OECD estimate. §Now using euro only. **Corrected.

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Global mergers and acquisitions

Mar 21st 2002
From The Economist print edition

Measured by their dollar value, fewer mergers and acquisitions are expected to have occurred in the first quarter of 2002 than in any other since 1996. Just over 2,000 deals are forecast.

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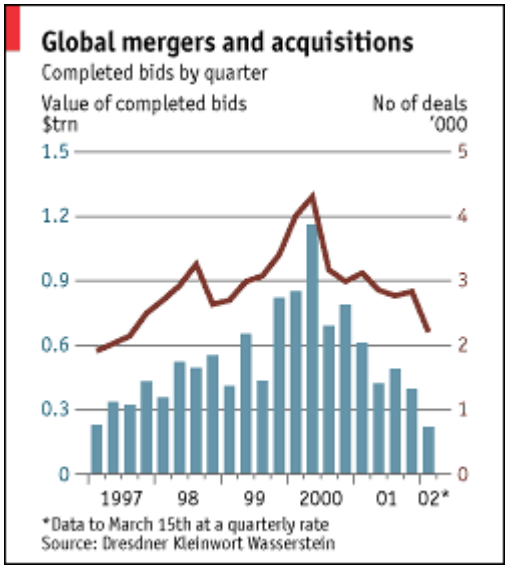

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Overview

Mar 21st 2002
From The Economist print edition

Strong consumer spending helped **South Korea's** economy to grow by 3.7% in the year to the fourth quarter. **Thailand's** GDP rose by 2.1% in the year to the fourth quarter.

South Africa's industrial production increased by 4.6% in the year to January. Annual consumer price inflation rose to 6.1% in February from 5.0% in January.

Argentina's industrial production sank by 15.6% in the year to February, because of the country's economic crisis.

Consumer prices in **Poland** rose by 3.5% in the year to February.

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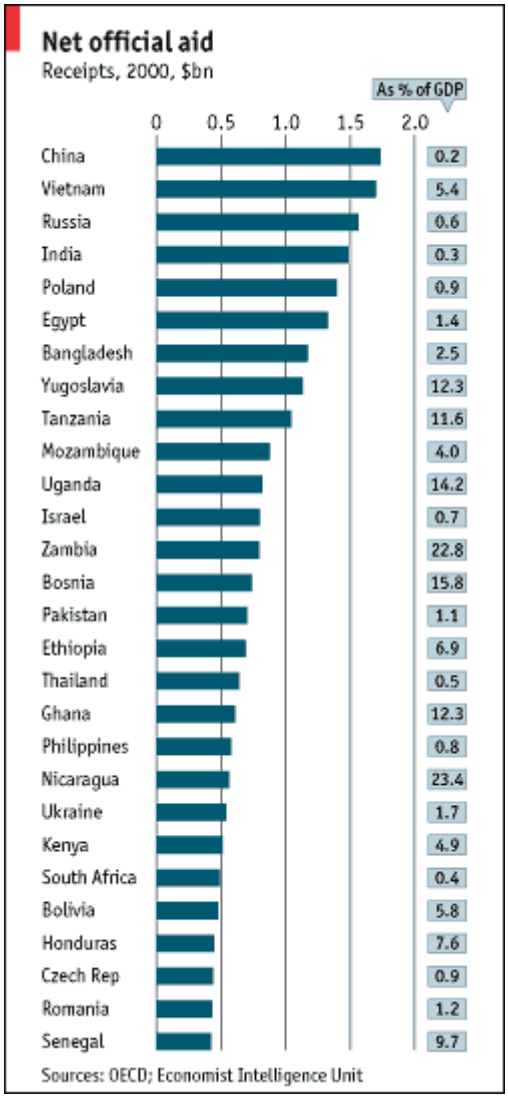
Net official aid

Mar 21st 2002
From The Economist print edition

The OECD's latest figures show that the amount of official aid countries receive varies widely. In dollar terms, China is the biggest beneficiary, receiving $1.7 billion in 2000. But as a share of GDP, that is a tiny 0.2%. Hit by natural disasters, Nicaragua received aid worth over 20% of GDP in 2000. Several countries, such as Israel, that are too rich to qualify for official development assistance, nonetheless receive substantial foreign aid for strategic reasons.



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Economy

Mar 21st 2002
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	% change on year earlier						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 6.6	Q4	+ 3.5	Feb	nil	Feb	+26.5	Feb	+20.5	2000	211.8	Nov
Hong Kong	– 1.6	Q4	– 7.1	Q3	– 3.5	Jan	–11.8	Jan	+ 8.9	Q3	111.3	Feb
India	+ 5.3	Q3	+ 3.2	Jan	+ 4.9	Jan	– 5.5	Jan	– 0.7	Q3	47.7	Feb
Indonesia	+ 4.1	Q4	+ 2.0	Q2	+15.1	Feb	+25.4	Jan	+ 3.8	Q3	27.0	Jan
Malaysia	– 0.5	Q4	– 6.7	Jan	+ 1.2	Feb	+14.5	Jan	+ 7.4	Q3	30.5	Dec
Philippines	+ 3.8	Q4	–11.3	Dec‡	+ 3.4	Feb	+ 2.8	Jan	+ 4.9	Nov	13.9	Feb
Singapore	– 7.0	Q4	+ 4.7	Jan	– 1.1	Jan	+ 5.7	Jan	+17.9	Q4	72.1	Feb
South Korea	+ 3.7	Q4	+10.2	Jan	+ 2.6	Feb	+ 9.4	Feb	+ 8.2	Jan	104.3	Jan
Taiwan	– 2.7	Q4	–11.5	Feb	+ 1.4	Feb	+17.9	Feb	+19.0	Q4	123.6	Jan
Thailand	+ 2.1	Q4	+ 1.3	Jan	+ 0.3	Feb	+ 2.6	Jan	+ 6.3	Jan	33.1	Jan
Argentina	– 4.9	Q3	–15.6	Feb	+ 4.0	Feb	+ 7.2	Jan	– 6.8	Q3	14.6	Dec
Brazil	– 0.7	Q4	– 1.3	Jan	+10.4	Feb	+ 3.5	Feb	–22.1	Jan	36.2	Jan
Chile	+ 2.6	Q3	+ 4.5	Jan	+ 2.5	Feb	+ 1.5	Feb	– 0.9	Q4	14.1	Jan
Colombia	+ 1.0	Q3	– 1.4	Dec	+ 6.7	Feb	+ 0.3	Dec	– 1.2	Q3	10.1	Jan
Mexico	– 1.6	Q4	– 3.3	Jan	+ 4.8	Feb	– 9.5	Jan	–17.1	Q4	47.2	Jan
Peru	+ 3.9	Jan	– 2.1	Dec	– 1.1	Feb	– 0.1	Jan	– 1.1	Q4	8.4	Jan
Venezuela	+ 2.8	Q3	+ 7.9	Oct	+13.7	Feb	+13.0	Q3	+ 4.4	Q4	9.2	Dec
Egypt	+ 4.6	2000†	+ 9.4	2000†	+ 2.5	Dec	– 8.6	Nov	nil	Q3	13.3	Nov
Israel	– 3.4	Q4	– 8.5	Dec	+ 4.0	Feb	– 6.7	Feb	– 1.7	Q4	24.2	Feb
South Africa	+ 1.8	Q4	+ 4.6	Jan	+ 6.1	Feb	+ 3.7	Jan	– 0.2	Q4	6.0	Jan
Turkey	– 7.1	Q3	– 3.1	Jan	+73.1	Feb	– 9.3	Dec	+ 3.3	Dec	19.1	Jan
Czech Republic	+ 3.2	Q4	+ 2.6	Jan	+ 3.9	Feb	– 3.1	Jan	– 2.7	Q4	14.7	Feb
Hungary	+ 3.3	Q4	– 0.6	Jan	+ 6.2	Feb	– 2.2	Jan	– 1.8	Jan	10.3	Jan
Poland	+ 0.8	Q3	+ 0.4	Feb	+ 3.5	Feb	–11.3	Jan	– 6.9	Jan	25.5	Feb
Russia	+ 4.9	Q3	+ 2.0	Feb	+17.9	Feb	+47.8	Jan	+41.5	Q3	32.8	Feb
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Pakistan	+ 3.3	2001†	+ 7.7	Sep	+ 2.5	Jan	– 1.0	Nov	+ 0.3	2001†	3.6	Jan
Saudi Arabia	+ 4.5	2000	na		nil	Dec	+50.9	2000	+14.3	2000	17.6	Jan

*Excluding gold, except Singapore; IMF definition. ‡New series. †Year ending June.

Text refers only to the first 25 countries listed

Sources: National statistics offices, central banks and stock exchanges; Thomson Financial Datastream; Economist Intelligence Unit; Reuters; Warburg Dillon Read; J.P Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; *Russian Economic Trends*.

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Financial markets

Mar 21st 2002
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Mar 20th		Dec 31st 2001	
	Mar 20th	year ago	Mar 20th	% p.a.		one week	in local currency	in $ terms
China	8.28	8.28	11.8	na	1,755.7	+3.7	+ 2.5	+ 2.5
Hong Kong	7.80	7.80	11.1	2.24	11,036.6	-1.6	- 3.2	- 3.2
India	48.7	46.7	69.5	6.05	3,581.3	+0.3	+ 9.8	+ 8.7
Indonesia	9,892	10,435	14,104	17.34	477.3	+0.7	+ 21.7	+ 28.0
Malaysia	3.80	3.80	5.42	3.28	755.0	+0.1	+ 8.5	+ 8.5
Philippines	51.1	48.5	72.9	7.69	1,407.5	+1.8	+ 20.5	+ 21.6
Singapore	1.83	1.78	2.61	1.06	1,801.9	+0.9	+ 11.0	+ 12.1
South Korea	1,321	1,303	1,883	4.77	887.5	+4.5	+ 27.9	+ 27.2
Taiwan	35.0	32.8	50.0	2.55	6,059.1	-0.5	+ 9.1	+ 9.0
Thailand	43.4	44.3	61.8	2.31	383.3	+1.2	+ 26.2	+ 28.7
Argentina	2.30**	1.00	3.28	na	412.0	+2.2	+ 39.5	- 39.4
Brazil	2.34	2.10	3.33	18.80	14,089.8	-0.9	+ 3.8	+ 2.7
Chile	658	586	939	4.68*	5,400.7	-0.7	+ 0.1	+ 0.5
Colombia	2,282	2,285	3,254	10.75	1,091.7	-2.3	+ 1.9	+ 1.7
Mexico	9.07	9.52	12.9	7.70	7,384.1	+2.3	+ 15.9	+ 17.1
Peru	3.46	3.52	4.93	2.33	1,322.1	+2.0	+ 12.5	+ 12.0
Venezuela	891	705	1,270	37.64	6,812.8	-1.5	+ 3.7	- 11.8
Egypt	4.63	3.88	6.61	7.21	5,402.9	+0.8	+ 2.5	+ 1.2
Israel	4.62	4.20	6.59	2.73	412.5	+3.9	- 7.7	- 11.9
South Africa	11.7	7.99	16.7	11.35	11,095.0	+0.6	+ 6.3	+ 9.1
Turkey	1,351,500	980,000	1,926,969	49.00	10,776.3	+1.7	- 21.8	- 15.8
Czech Republic	35.4	38.5	50.4	4.30	418.4	-4.9	+ 6.0	+ 6.6
Hungary	276	297	394	8.40	7,858.3	-2.6	+ 10.2	+ 9.6
Poland	4.10	4.12	5.85	10.55	14,813.3	-2.0	+ 6.4	+ 2.6
Russia	31.2	28.7	44.5	25.00	340.8†	+5.6	+ 34.0	+ 31.0
EMF (MSCI)‡	1.00	1.00	1.43	na	350.5	+0.9	na	+ 10.4
EMBI+§	1.00	1.00	1.43	na	213.9	+0.2	na	+ 6.7

*New series. †In $ terms. ‡Emerging Mkts Free. §J.P. Morgan Chase's Emerging Mkts Bond Index Plus. **Fixed official rate 1.40.
Sources: National statistics offices, central banks and stock exchanges; Thomson Financial Datastream; Economist Intelligence Unit; Reuters; Warburg Dillon Read; J.P Morgan Chase; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; FIEL; EFG-Hermes; Bank Leumi Le-Israel; Standard Bank Group; Garanti Bank; Deutsche Bank; *Russian Economic Trends*.

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